CANADIAN PACIFIC 1998 ANNUAL REPORT

EXPANDING OUR HORIZONS

CANADIAN PACIFIC

Energy Transportation Hotels

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Canadian Pacific Limited

Calgary-based Canadian Pacific is a diversified operating company active in transportation, energy and hotels. The Canadian Pacific group of companies includes Canadian Pacific Railway, CP Ships, PanCanadian Petroleum, Fording and Canadian Pacific Hotels.

1999 Annual Meeting

The Annual Meeting of Shareholders will be held on Tuesday, April 20, 1999 at The Palliser Hotel, 9th Avenue and 1st Street South West, Calgary, Alberta, at 11:00 a.m., Calgary time.

EXPANDING OUR HORIZONS In the last two years, we have dramatically expanded our shipping and hotel businesses beyond their traditional Canadian base. At CP Ships, we moved beyond our Montreal gateway in 1997 with the acquisition of Lykes Lines based in Tampa, Florida and Contship Containerlines based in Ipswich, England. In 1998, we further broadened our scope and reach with the acquisition of Ivaran Lines and Australia-New Zealand Direct Line (ANZDL). We also

completed a major joint venture with Transportación Marítima Mexicana (TMM) in early 1999 that will be managed from Tampa, Florida. Through these acquisitions and our existing operations, we now have a major presence in three regional markets: the North Atlantic, Latin America and Australasia. We have over 50 ships in our fleet and call at more than 80 ports around the world. The map on the following page illustrates our major trade lanes and lists some of the countries that we serve.

With the commencement of the TMM venture in early 1999, we will carry approximately 1.4 million twenty-foot equivalent units (teus) per year, up from just over 240,000 teus five years ago. This volume will make us one of the top ten container shipping companies in the world – a remarkable accomplishment considering our size five years ago and the fact that we do not compete in the largest trade lanes – the Trans-Pacific and Asia-Europe.

CP Ships' Routes

Countries Served by CP Ships:

Argentina
Australia
Barbados
Brazil
Belgium
Canada
Canary Islands
Colombia
Costa Rica
Dominican Republic
Ecuador
Egypt
Fiji
France
Germany
Greece
Guam
India
Indonesia
Italy
Japan
Jordan
Mexico
Netherlands
New Caledonia
New Zealand
Pakistan
Portugal
Puerto Rico
Saudi Arabia
Singapore
South Africa
Spain
Sri Lanka
Tahiti
United Arab Emirates
United Kingdom
United States
Uruguay
Venezuela

The transformation of Canadian Pacific Hotels has been just as exciting. In 1997, the creation of Legacy Hotels Real Estate Investment Trust and the sale of trust units provided $642 million for expansion and significantly reduced our capital intensity. In 1998, Canadian Pacific Hotels dramatically expanded. In the second quarter, we further strengthened our Canadian presence with the purchase of Delta

Hotels as well as two additional hotels in the Toronto area. The Delta purchase doubled our rooms under management and gave us a platform for growth in another segment of the Canadian hotel market, just under our existing Canadian Pacific Hotels brand. In August, we purchased Princess Hotels which expanded our network beyond Canada to the U.S., Mexico, Bermuda and the Caribbean. We have now

become the fourth largest resort hotel operator in North America and the Caribbean. The Princess Hotels acquisition gives us warm weather resort properties that fit well with our existing resort portfolio and provides strong growth opportunities. The map below demonstrates the growth Canadian Pacific Hotels has experienced in 1998 as we increased our hotels under management from 26 to 65 and our rooms

under management from 10,000 to over 25,000. In both our shipping and hotel businesses, we have broadened our base and become much more international in our outlook. We believe that this will enable us to create many more opportunities for profitable growth as both container shipping, and hotels and tourism are rapidly growing industries in an increasingly global market.

Financial Highlights

(in millions – except per share amounts)	**1998**	1997	1996
Income Items			
Revenues from continuing operations	**$ 10,151.0**	$ 9,560.0	$ 8,471.3
Operating income			
Canadian Pacific Railway	**$ 736.0**	$ 802.1	$ 603.0
CP Ships	**161.2**	145.6	110.9
PanCanadian Petroleum	**236.4**	484.7	474.8
Fording	**129.2**	197.0	162.5
Canadian Pacific Hotels and Real Estate Activities	**178.9**	136.3	115.8
	$ 1,441.7	$ 1,765.7	$ 1,467.0
Net income from continuing operations	**$ 801.3**	$ 946.7	$ 840.0
Net income	**$ 801.3**	$ 1,255.8	$ 869.1
Per Common Share			
Net income from continuing operations	**$ 2.39**	$ 2.74	$ 2.44
Net income	**$ 2.39**	$ 3.64	$ 2.52
Cash flow	**$ 6.03**	$ 6.34	$ 5.78
Dividends	**$ 0.54**	$ 0.48	$ 0.48
Market price at December 31 (Toronto Stock Exchange)	**$ 28.75**	$ 38.50	$ 36.05
Rates of Return			
Average shareholders' equity – continuing operations	**10.3%**	13.2%	13.1%
Average capital employed (operating)	**9.8%**	14.0%	11.9%
Financial Condition			
Cash flow	**$ 2,024.8**	$ 2,189.4	$ 1,991.0
Capital expenditures	**$ 2,337.1**	$ 2,465.0	$ 1,641.1
Cash on hand, net	**$ (282.4)**	$ 444.4	$ 852.6
Total long term debt	**$ 3,462.6**	$ 2,855.6	$ 3,441.8
Net debt	**$ 3,745.0**	$ 1,779.2	$ 2,589.2
Shareholders' equity	**$ 7,998.0**	$ 7,573.4	$ 6,727.8
Total assets	**$ 19,669.4**	$ 17,331.9	$ 15,805.9
Net debt:equity ratio	**31 : 69**	18 : 82	27 : 73
Common Share Capital			
Average number of shares outstanding *(in millions)*	**335.8**	345.4	344.4
Number of registered shareholders at December 31	**37,172**	41,165	38,525
Number of Employees			
Average for the year	**39,804**	33,600	34,200

1998 Highlights

In 1998,

we improved

the competitive

positions

of our

businesses.

Strengthening our Canadian base

Improved Canadian Pacific Railway's operating ratio to 79.2%

Increased gas production on PanCanadian's gas-prone fee lands

Acquired Delta Hotels

Completed $2.3 billion capital program

Expanding our horizons

Acquired Princess Hotels

Expanded Latin American shipping presence with Ivaran Lines acquisition and joint venture with Transportación Marítima Mexicana

Extended Australasian shipping platform with Australia-New Zealand Direct Line acquisition

Maintaining financial strength

Achieved record results in rail, shipping and hotel businesses

Exceeded $2 billion in cash flow

Net debt to equity ratio of 31:69

Letter to Shareholders

Canadian Pacific's rail, shipping and hotel businesses all recorded substantial achievements in 1998. We made major progress improving the competitive positions of each of these businesses and, as detailed elsewhere in this report, we dramatically expanded our shipping and hotel operations beyond their traditional Canadian base.

Our energy businesses, on the other hand, were seriously affected by Asian economic difficulties which reduced demand and triggered a significant decline in oil and coal prices. Crude oil prices were almost in free-fall and, on an inflation-adjusted basis, dropped to levels not seen since the 1973 beginnings of OPEC influence in oil markets. The impact of falling commodity prices and soft markets on our energy businesses more than offset our growing earnings in other segments.

FINANCIAL RESULTS

Our financial performance deteriorated in 1998. Combined net earnings of our rail, shipping and hotel businesses were better than in 1997 but a significant decline in earnings at PanCanadian and Fording, combined with lower gains from special items, reduced total earnings per share from continuing businesses to $2.39 compared with $2.74 in 1997.

Revenues were up 6% to $10.2 billion compared with $9.6 billion in 1997. Cash flow per share was $6.03, down 5% from $6.34 per share in 1997. Our year-end net debt ratio of 31:69 and net debt-to-cash-flow ratio of 1.8:1 reflect our solid financial position. During 1998, capital expenditures and acquisitions totalled over $3.5 billion, and nearly nine million shares were purchased at a cost of $325 million.

OPERATING PERFORMANCE

Canadian Pacific Railway continued to focus on cost cutting, franchise renewal and revenue growth through improved customer service. The railway's operating income, excluding special items, increased to a record $721 million from $668 million in 1997 and its operating ratio fell below 80% for the first time. Higher intermodal, automotive and forest products revenues mitigated weakness in demand for some bulk commodities, particularly grain and coal. In 1998, the railway reduced operating expenses by over $160 million as a result of a system-wide effort to improve efficiency and drive down costs.

At over $1 billion, capital expenditures in 1998 were the highest in the railway's four-year infrastructure and locomotive renewal program. New AC-traction locomotives have been a big part of the program. By the end of 1998, the railway had

received 210 locomotives which resulted in reduced maintenance and fuel costs and lower equipment rents. The revitalized fleet, coupled with major track upgrades in high-volume corridors, led to improved train speed and reliability. Investment in four terminals increased intermodal handling capacity by 125,000 loads in 1998 and will add another 105,000 loads in 1999, an overall increase of 60%. During 1998, a new terminal in Calgary opened and the Vaughan terminal in Toronto was expanded. In 1999, a new Vancouver terminal will open and expansion of a terminal in Montreal will be completed. Another part of the renewal program is the implementation of powerful new computer applications which will generate reliable, real-time information with which to plan and deliver railway service. With these new tools, assets will be used more productively, maximizing the recent investments in locomotives, track and terminals.

In conjunction with these initiatives, a focus on top-line revenue growth is being driven by an unwavering commitment to improved customer service. On-time performance, train speeds, locomotive productivity and safety performance have reached record levels. The result has been more efficient service, smoother freight flows through the system and, most importantly, increased customer satisfaction.

CP Ships had another record year despite difficult market conditions that put pressure on rates and volumes. Operating income increased to $161 million from $146 million in 1997 on the strength of lower costs and increased carryings related to acquisitions. The benefits of its ambitious expansion program began to surface during the year as Lykes Lines, Contship Containerlines and Ivaran Lines were integrated into existing operations, providing opportunities to improve service and realize synergies among lines. At the same time, CP Ships lowered the cost structure of its existing businesses, Canada Maritime and Cast, by investing in new ships and its terminals at the Port of Montreal. With the acquisition of Australia-New Zealand Direct Line in December 1998, CP Ships significantly increased its market share in Australasia. During 1998, the company's ongoing efforts to drive down costs, improve organizational effectiveness and provide better service allowed it to maintain a low-cost position in its regional markets and offset the impacts of a difficult rate environment.

Cash flow at PanCanadian decreased to $802 million from $961 million in 1997 and operating income decreased to $236 million from $485 million. Low crude oil prices were only partially offset by higher natural gas production and prices and a reduction in operating costs.

Faced with deteriorating business conditions, PanCanadian focused on reducing operating and development costs and increasing profitable production, particularly in natural gas. The company implemented an aggressive natural gas development program in Western Canada to take advantage of its gas-prone fee lands, its proximity to the transportation infrastructure, increasing pipeline capacity, a favourable pipeline tariff and rising demand in the U.S. Newly-formed business units began an in-depth review of their properties to identify the most profitable opportunities. During the year, operating costs were reduced 18% and the workforce was cut by approximately 10%.

In addition to its Western Canadian activities, PanCanadian continued to widen its search for new oil off Canada's east coast and in the Gulf of Mexico. The Llano well discovered in June in the Gulf of Mexico is a significant prospect and PanCanadian has an interest in a number of other prospects in the same area.

Fording's operating income dropped to $129 million from $197 million in 1997. International coal markets proved extremely challenging as Asian steel production declined and a lower Australian dollar made Australian coal exports more competitive internationally. Contract prices and volumes with the Japanese steel mills declined significantly as did spot sales volumes and prices. In this difficult environment, Fording continued to focus on diversifying its markets and enhancing its status as a low-cost producer. Losses related to the start-up of the new wollastonite mine in Mexico and slow sales prompted Fording to intensify its efforts to increase market share and develop new applications.

Canadian Pacific Hotels, taking advantage of a strong domestic economy, a weak Canadian dollar and increasing international tourism, had record operating income of $148 million, compared with $136 million in 1997. Weakness in Asian tourism was offset by increased demand from U.S., European and Canadian markets. The Canadian resort properties and the Legacy business hotels achieved higher occupancy rates and higher average room rates, while the Delta and Princess hotels, acquired in 1998, made positive contributions.

THE WAY FORWARD

The impact of declining economic activity in Asia and elsewhere will continue to be felt in 1999. The Japanese steel mills' price for metallurgical coal in the next coal year commencing April 1, 1999 will be U.S.$41.45 or 18% lower than the 1998 price. All indications suggest that oil prices will remain at low levels compared with recent years. Lower coal prices and depressed prices for other bulk commodities will also have a negative impact on rail revenues.

These challenging conditions require us to rethink our directions and take steps to reduce our costs, improve our profitability and, where necessary, shift our business mix.

We have already moved in this direction. During 1998, PanCanadian placed increasing emphasis on natural gas, growing production by 7% to 796 million cubic feet per day. In 1999, PanCanadian's capital program will be directed largely to growing our natural gas business. At the same time, we have fixed the prices on about two-thirds of our gas production for the first ten months of 1999 at extremely attractive prices. We are also aggressively reducing costs in our oil business so that our cost structure will be consistent with the new pricing realities, and we are substantially reducing capital directed to oil which will result in lower oil production. Our focus is on maximizing the cash flow from our oil production.

Canadian Pacific CEOs

David Tuer
PanCanadian

Rob Ritchie
Canadian Pacific Railway

Ray Miles
CP Ships

David O'Brien
Canadian Pacific

Bill Fatt
Canadian Pacific Hotels

Jim Gardiner
Fording

Canadian Pacific Railway will continue to concentrate on cost reduction, asset renewal and service reliability. The railway is in the final year of a four-year capital catch-up program that will produce cost savings and greater operating efficiencies in 1999 and beyond. In addition, we will focus on increasing traffic density in our major rail corridors.

We anticipate substantial growth in profitability at Canadian Pacific Hotels as we benefit from the first full year of the Princess and Delta acquisitions. At CP Ships, we expect major cost reductions as we integrate our new acquisitions and realize synergies from our joint venture with Transportación Marítima Mexicana which has an effective date of January 1, 1999.

A difficult external environment produces both challenges and opportunities and we expect there will be new opportunities in 1999 to grow our businesses. In addition, as we move forward, we will continue to reduce our capital intensity, narrow our business focus, and surface the value in real estate and other non-core assets.

A WORLDWIDE FAMILY

As our businesses expand in the international marketplace, the Canadian Pacific family is growing not just in Canada but around the world. In 1998, we welcomed new employees at Ivaran Lines, Australia-New Zealand Direct Line, Delta Hotels and Princess Hotels. Today, our employee base is broader than it has ever been. The skills and dedication of this diverse group of people will be an invaluable resource as we take on new challenges in different parts of the world.

Four directors will retire from our Board at the annual meeting in April. Bill Stinson has been a director since 1981 and was chief executive officer of the Corporation from 1985 to 1996. During that time, he initiated the restructuring of Canadian Pacific and improved the competitive positions of our businesses. Stanley A. Milner, our longest-serving director, joined the Board in 1980. He has been closely involved in the affairs of the Corporation, serving with distinction as Chairman of the Management Resources and Compensation Committee and the Corporate Governance and Nominating Committee. In his role as Chairman of the latter committee, he has acted as lead director since 1995. The Hon. Peter Lougheed has been a director since 1986. His distinguished career in public service has enabled him to bring a unique and valuable perspective to the Board. James A. Pattison, a director since 1991, is one of Canada's leading entrepreneurs and we have benefited from his broad business experience. During his tenure, he served on a variety of committees, including the Executive Committee.

We thank all of these men for their significant contributions to the affairs of the Corporation over many years.

David P. O'Brien
Chairman, President
and Chief Executive Officer

February 8, 1999

Questions and Answers

Chairman, President and Chief Executive Officer David O'Brien answers questions about issues facing the company, current initiatives and future directions.

Q. Canadian Pacific Hotels has expanded from 26 to 65 hotels over the last year – what is its future strategy and direction?

Let me say at the outset that tourism is one of the fastest growing global industries and we plan to benefit from that growth both here in Canada and internationally. Our strategy for Canadian Pacific Hotels is threefold.

First, we wish to focus principally on the business of hotel management and to make new investments in real estate only as required to expand our management business. In late 1997 we sold 11 of our business hotels to the Legacy REIT which allowed us to surface the real estate value in these properties while maintaining long term management contracts. In the first half of 1998 we purchased Delta Hotels, a hotel management company with management contracts mainly in Canada.

Second, as part of our hotel management strategy, we wish to develop brand names in more than one segment of the market. Delta provides Canadian Pacific Hotels with a solid entry into a new market segment through an established brand positioned just below the Canadian Pacific Hotels brand.

Third, we want to develop our hotel business in North America and beyond, in both the business and resort sectors. In order to create a platform for growth beyond Canada, we purchased Princess Hotels in August 1998. This acquisition makes Canadian Pacific Hotels the fourth largest resort operator in North America and the Caribbean. We will now focus on creating a brand for our Four Star Plus product that will be recognized internationally, enabling us to compete for hotel management contracts and build a growing and profitable business that provides superior returns on invested capital.

Q. Canadian Pacific Railway has made significant progress in cutting costs and lowering its operating ratio – where do you go from here?

We have several elements to our strategy going forward:

First, we will effectively complete the last year of our four-year capital catch-up program, which we began in 1996. We have already begun to see the economic benefits of increased system capacity, a more competitive cost structure, and better and more reliable service offerings.

As well, we will continue to work on the dual goals of cost reduction and revenue growth. We still have room for substantial reduction in our cost structure both through improved asset utilization and increased labour

productivity. We now have the infrastructure in terms of track, terminals, yards and locomotives to increase our carryings and revenues. In the last year, we have succeeded in increasing our intermodal market share given our improved service levels. We see substantial opportunities to build traffic on our Vancouver to Chicago corridor as well as in the U.S. northeast arising from our new access to major metropolitan areas such as New York, as well as through our north/south links with Norfolk Southern.

Our third focus is to improve our return on the capital invested in the business. Like many railroads, we have been concentrating on driving down our operating ratio. In fact, in 1998, we achieved an operating ratio below 80% for the first time. Operating ratio is not, however, a full reflection of the ability of a railway to earn a return in excess of the cost of capital. We are focused on reducing the capital intensity of the business and disposing of non-core assets such as excess real estate. With the completion of our four-year capital catch-up program in 1999, our principal objectives are to earn a return above the cost of capital and to generate free cash flow after required capital expenditures. As part of this strategy, we plan to increase our scale, scope and reach, not by capital intensive acquisition but through business partnerships with other Class 1 North American railways where we work together to provide improved service to our customers across North America.

David P. O'Brien
Chairman, President and Chief Executive Officer

Q. What are the short and medium term implications of the deterioration of the Asian economies on the businesses of Canadian Pacific?

The Asian flu has, in the short term, caused a precipitous decline in the price of oil, coal and other commodities. The negative impacts were felt almost immediately in reduced profitability at PanCanadian and Fording and, to a lesser extent, at Canadian Pacific Railway in terms of bulk commodity revenues. The toughest year in a soft pricing environment is normally the first year because we have little opportunity in the short term to reduce our cost structure to reflect the new realities. In 1999, we will have realigned our operations and shifted our business mix to reduce the negative impacts.

In the medium term, over-capacity in Asia will be rationalized and capital will be more carefully allocated to projects capable of generating economic profit. We believe this will have positive implications in terms of reducing shipbuilding capacity and increasing profit margins in the shipping industry. We also believe that the problems in Asia will open up new opportunities for investment in that region in some of our core businesses.

Transportation

Canadian Pacific Railway

moves 150 million tons of goods annually across Canada and in the U.S. midwest and northeast.

Canadian Pacific Railway

Canadian Pacific Railway provides rail and intermodal freight transportation services over a 15,300-mile network extending from Montreal to Vancouver and into the U.S. midwest and northeast. It serves ports on the east coasts of Canada and the U.S. and the Port of Vancouver, moving large volumes of import and export goods across the continent. Canadian Pacific Railway is also a leading carrier in the intermodal industry with 23 terminals across Canada and the northern U.S.

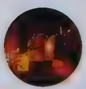
CP Ships

is one of the ten largest container shipping companies in the world.

CP Ships

CP Ships operates in three key regional markets: the North Atlantic, Latin America and Australasia. CP Ships is comprised of six container shipping companies: Canada Maritime, Cast, Lykes Lines, Contship Containerlines, Ivaran Lines and Australia-New Zealand Direct Line. In early 1999, CP Ships and Transportación Marítima Mexicana (TMM) formed Americana Ships, a joint venture to merge the container shipping businesses of TMM, Lykes Lines and Ivaran Lines. CP Ships also operates CP Ships Logistics and Montreal Terminals.

Energy



PanCanadian Petroleum

is a leading Canadian oil and gas producer.

PanCanadian Petroleum

PanCanadian is one of Canada's largest producers and marketers of crude oil, natural gas and natural gas liquids. Its extensive exploration and production activities stretch from coast to coast in Canada and include a variety of international interests in the Gulf of Mexico, the United Kingdom, Australia, Africa and Venezuela. PanCanadian has been among Canada's most active and successful drillers for a number of years.

Fording

sells metallurgical coal to countries around the world.

Fording

Fording is Canada's largest and lowest-cost producer of export coal. Its three mines in southeastern British Columbia produce primarily high-quality metallurgical coal for the international steel industry. Its operations in Alberta include two mines supplying thermal coal to local electric utilities, and an oil-sand overburden removal operation. Fording is also the world's largest producer of the industrial mineral wollastonite.

Hotels

Canadian Pacific Hotels

is the fourth largest destination resort operator in North America.

Canadian Pacific Hotels

Canadian Pacific Hotels is Canada's largest owner-operator of full service hotels with 65 hotels and over 25,000 rooms across Canada, the United States, Mexico, Bermuda and Barbados. It operates under two distinct brands, Canadian Pacific Hotels and Delta Hotels, positioning it as a major international hotel company in the luxury and mid-market hotel segments.

	1998	1997	1996
Revenues *(millions)*	**$ 3,516.5**	$ 3,716.8	$ 3,559.4
Operating income *(millions)*	**$ 736.0**	$ 802.1	$ 603.0
Net income *(millions)*	**$ 367.4**	$ 416.7	$ 445.4
Cash flow *(millions)*	**$ 761.2**	$ 732.5	$ 675.8
Revenue ton miles *(billions)*	**102.2**	105.8	103.4
Trackage *(miles)*	**15,900**	15,900	17,400
Locomotives	**1,641**	1,619	1,615
Freight cars	**51,900**	53,000	54,000
Active employees	**19,860**	20,150	21,730

	1998	1997	1996
Revenues *(millions)*	**$ 2,646.7**	$ 1,475.8	$ 1,113.8
Operating income *(millions)*	**$ 161.2**	$ 145.6	$ 110.9
Net income *(millions)*	**$ 151.3**	$ 134.7	$ 103.5
Cash flow *(millions)*	**$ 217.6**	$ 184.8	$ 134.8
Container carryings*	**1,160**	671	480
Employees	**3,244**	1,500	1,300

* *thousand twenty-foot equivalent container units*

	1998	1997	1996
Revenues *(millions)*	**$ 2,965.6**	$ 3,238.6	$ 2,744.2
Operating income *(millions)*	**$ 236.4**	$ 484.7	$ 474.8
Net income *(millions)*	**$ 116.6**	$ 273.7	$ 285.6
Cash flow *(millions)*	**$ 801.9**	$ 961.4	$ 1,000.8
Wells drilled*	**1,079**	1,820	1,221
Total reserves – conventional oil and natural gas liquids†	**547**	637	422
Total reserves – natural gas†	**362**	361	341
Employees	**1,785**	2,000	1,700

* *working interest*
† *million barrels of oil equivalent – proved plus probable, before royalty (natural gas converted at a rate of 10,000 cubic feet to one barrel of oil)*

	1998	1997	1996
Revenues *(millions)*	**$ 906.1**	$ 1,017.8	$ 915.1
Operating income *(millions)*	**$ 129.2**	$ 197.0	$ 162.5
Net income *(millions)*	**$ 65.9**	$ 117.7	$ 93.6
Cash flow *(millions)*	**$ 142.8**	$ 227.0	$ 160.0
Cleaned coal sales *(thousand tonnes)*	**12,360**	13,540	12,100
Proven and probable reserves *(million tonnes)**	**3,770**	3,770	3,895
Employees	**1,955**	1,900	1,800

* *includes metallurgical and thermal coal, wollastonite, tripoli and potash*

	1998	1997	1996
Revenues *(millions)*	**$ 518.5**	$ 565.1	$ 565.6
Operating income *(millions)*	**$ 147.9**	$ 136.3	$ 115.8
Net income *(millions)*	**$ 81.6**	$ 163.3	$ 70.0
Cash flow *(millions)*	**$ 116.5**	$ 123.5	$ 84.4
Hotels	**65**	26	26
Rooms	**25,617**	11,429	11,100
Employees *(full-time equivalent)*	**12,800**	7,900	7,400

Operating Income

CANADIAN PACIFIC RAILWAY 51%
CP SHIPS 11%

PANCANADIAN PETROLEUM 16%
FORDING 9%
CANADIAN PACIFIC HOTELS AND REAL ESTATE ACTIVITIES 13%

Revenues

CANADIAN PACIFIC RAILWAY 33%
CP SHIPS 25%

PANCANADIAN PETROLEUM 28%
FORDING 9%
CANADIAN PACIFIC HOTELS AND REAL ESTATE ACTIVITIES 5%

Assets

CANADIAN PACIFIC RAILWAY 43%
CP SHIPS 9%

PANCANADIAN PETROLEUM 32%
FORDING 6%
CANADIAN PACIFIC HOTELS AND REAL ESTATE ACTIVITIES 10%

Positioned in Three Key Regional Markets

CP Ships has expanded beyond its traditional Montreal Gateway. It now operates in three key regional markets: the North Atlantic, Latin America and Australasia and is positioned for strong and growing profitability as world trade expands.

Adding a Warm Weather Dimension

Through the acquisition of Princess Hotels, Canadian Pacific Hotels has added warm weather properties that complement its existing resort portfolio. This acquisition is a significant step in expanding its resort business and moving beyond Canada.

A Revitalized Railway

Canadian Pacific Railway is three-quarters of the way through its asset renewal and revitalization program and has begun to see the benefits of increased system capacity, a more competitive cost structure and better service offerings.

Operating in a Tough Environment

PanCanadian is concentrating on its traditional strategic advantage – exploring and developing its strong land position in Western Canada, particularly its gas-prone fee lands while continuing to focus on reducing finding and development and operating costs.

Diversifying Markets

Given difficult coal markets, Fording is focused on diversifying its markets and maintaining its position as Canada's lowest-cost metallurgical coal exporter.

CANADIAN PACIFIC IN THE COMMUNITY We at Canadian Pacific believe that we have a responsibility to the communities in which our employees live and work and where we operate our businesses. Canadian Pacific has been making a difference in communities across Canada for more than a century. The Canadian Pacific Charitable Foundation was established in 1994 to more effectively target and administer

our community investment activities. In 1998, the Canadian Pacific Charitable Foundation made $6.5 million of grants to worthy organizations such as the United Way/Centraide campaigns, educational organizations, arts and culture groups and hospitals across the country. In addition, PanCanadian on its own donated $1.5 million.

(the Corporation) and all of its subsidiaries is supplemental to the consolidated financial statements and related notes contained in the 1998 Annual Report to Shareholders. The financial statements for the year ended December 31, 1998 were prepared in accordance with generally accepted accounting principles (GAAP) in Canada. Differences from GAAP in the United States are disclosed in Note 23 on pages 96, 97, 98 and 99 of the Annual Report.

Management's Discussion and Analysis

1998 was another year of solid progress for Canadian Pacific. Despite a difficult business environment, the Corporation extended its operations internationally while further strengthening its businesses in Canada.

Canadian Pacific Railway made significant progress in its cost-based turnaround and revitalization program, reporting better results and establishing a strong basis for future revenue growth. For the first time, the railway achieved an operating ratio below 80%. CP Ships continued to focus on realizing operating synergies among its lines, reducing its overall cost structure and enhancing its services. Canadian Pacific Hotels broadened its coverage in the Canadian market with the Delta Hotels acquisition and improved performance at its flagship Canadian properties, achieving higher occupancy and room rates.

The energy businesses faced difficult markets in 1998. In response, PanCanadian shifted its emphasis to natural gas, Fording further diversified its customer base and both put a renewed focus on controlling costs to maintain their strong competitive positions among producers in Canada.

During the year, Canadian Pacific expanded its shipping and hotel businesses internationally. CP Ships established a strong presence in Latin American and Australasian trades with acquisitions and the announcement of a joint venture. Canadian Pacific Hotels expanded its resort portfolio beyond Canada to the U.S., Mexico and the Caribbean.

Today, with a strong Canadian base and an increasing international presence, Canadian Pacific is well positioned to deal with new opportunities and challenges as it moves into the 21st century.

1998 BUSINESS ENVIRONMENT

In 1998, oil and coal markets were particularly depressed by the weakness in the Asian economies. This significant decline in demand adversely affected oil prices at PanCanadian and reduced both prices and sales volumes of coal at Fording. Bulk commodity shipments at Canadian Pacific Railway, particularly coal traffic, were also impacted, but other shipments were stronger as the North American economies remained generally healthy. CP Ships was relatively unaffected by the downturn in Asia because it does not compete in the Trans-Pacific and Asia to Europe trade lanes. However, overcapacity in the ocean shipping industry continued to exert competitive pressure on freight rates and carryings. Canadian Pacific Hotels benefited from the favourable economic situation in North America, with demand further stimulated by the relative weakness of the Canadian dollar.

RECORD RESULTS IN THREE BUSINESSES

Record results at Canadian Pacific Railway, CP Ships and Canadian Pacific Hotels narrowed the decline in consolidated net income from continuing operations excluding special items to less than 10%. Better results in the transportation and hotel businesses were principally attributable to cost saving initiatives and an expanded business base. Weak oil and coal markets led to a decrease of over 50% in net income, excluding special items, from the energy businesses in 1998 versus 1997.

Income Excluding Special Items

(in millions – except per share amounts)	**1998**	1997	1996
Operating income			
Canadian Pacific Railway	**$ 721**	$ 668	$ 586
CP Ships	**161**	146	111
PanCanadian Petroleum	**237**	485	475
Fording	**129**	197	162
Canadian Pacific Hotels and Real Estate Activities	**179**	136	116
	$ 1,427	$ 1,632	$ 1,450
Net income			
Canadian Pacific Railway	**$ 347**	$ 317	$ 325
CP Ships	**151**	135	104
PanCanadian Petroleum	**116**	274	286
Fording	**66**	118	94
Canadian Pacific Hotels and Real Estate Activities	**99**	63	50
Other activities	**2**	(47)	(112)
Net income from continuing operations	**$ 781**	$ 860	$ 747
Per Common Share	**$ 2.32**	$ 2.49	$ 2.17

EXTENDING OPERATIONS INTERNATIONALLY

The expansion into international markets included the entry of CP Ships into two new trade lanes – North America to Central and South America, as well as Europe and North America to Australasia. CP Ships acquired Ivaran Lines, operating in the Caribbean and South America. The company also acquired Australia-New Zealand Direct Line (ANZDL) which, combined with Contship Containerlines purchased in 1997, will establish a leading presence in the Australasia trade. Early in 1999, CP Ships reached an agreement to form a joint venture of its Lykes Lines and Ivaran Lines with Transportación Marítima Mexicana (TMM) to create a solid foothold in Latin American markets. The 50/50 joint venture will be called Americana Ships.

Canadian Pacific Hotels built on its strong position in the destination hotel segment with the purchase of Princess Hotels, which has properties in Mexico, Bermuda, Barbados and Arizona. The Princess acquisition complements the company's existing resort properties by adding a warm weather dimension. It is also an important platform for future growth in response to what is expected to be growing demand in the resort tourism industry.

STRENGTHENING THE CANADIAN BASE

Substantial progress was made during the year to increase the efficiency of the core businesses and improve their growth prospects. This was achieved through a focus on controlling costs and by investing capital to improve efficiency.

At Canadian Pacific Railway, over $1 billion was spent to revitalize its infrastructure, including its locomotive fleet, track and terminals. The railway, in the third year of a four-year revitalization program, began to benefit from increased system capacity, a more competitive cost structure, better service, and revenue growth opportunities. The full benefits of the program are expected to be realized over the next several years.

CP Ships successfully turned around Lykes Lines, an East Coast U.S. container shipping company acquired in the third quarter of 1997, and produced cost savings at Canada Maritime and Cast to help offset competitive pressure on rates and volumes.

Canadian Pacific Hotels expanded its management of business hotels in Canada with the acquisition of Delta Hotels which is positioned in the higher-end, mid-market segment. This acquisition not only provides a solid entry into a new market segment through an established brand but also offers opportunities for synergies in the centralization of support functions and revenue enhancements.

In 1998, PanCanadian realigned its business units to focus on reducing operating costs and directing efforts to its traditional strategic advantage – exploring and developing its strong land position in Western Canada, particularly its fee land legacy. PanCanadian's unit operating costs on working interest production were reduced by almost 20% and gas production increased 7% in 1998.

Fording's coal operations benefited from its high productivity position to keep production costs low. Fording also continued its strategy of diversifying sales markets to offset some of the dependence on customers in Asia, with sales to these customers down to 51% of total shipments in 1998 from 77% in 1993.

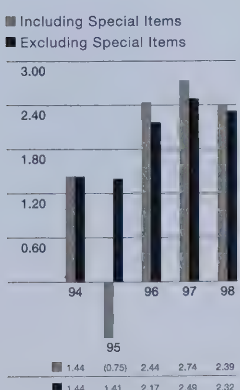
Consolidated Results

Even though oil prices started to decline in mid-1997, it was their continued weakening through 1998, coupled with poor coal markets, that overshadowed the stronger results from the transportation and hotel businesses in 1998 and 1997. Excluding special items, consolidated net income from continuing operations was $781 million, or $2.32 per Common Share, in 1998 compared to $860 million, or $2.49 per Common Share, in 1997 and $747 million, or $2.17 per Common Share, in 1996. Consolidated operating income, excluding special items, amounted to $1,427 million in 1998, compared with $1,632 million in 1997 and $1,450 million in 1996. The Corporation's revenues amounted to $10,151 million in 1998, up $591 million over 1997 and $1,680 million over 1996. The increase in revenues was chiefly attributable to growth at CP Ships.

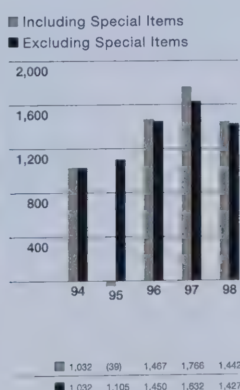
The return on average shareholders' equity from continuing operations, excluding special items, was 10.0% in 1998, 12.0% in 1997 and 11.6% in 1996. The return on average capital employed was 9.7%, 12.9% and 11.7% in 1998, 1997 and 1996, respectively, when adjusted to exclude special items.

Results were also affected, particularly in 1997, by special items that arose principally from the Corporation's disposition of non-core assets. Consolidated net income from continuing operations including special items was $801 million, or $2.39 per Common Share, in 1998 and was down from $947 million, or $2.74 per share, in 1997 and $840 million, or $2.44 per share, in 1996. On this basis, the Corporation's operating income was $1,442 million in 1998 down from $1,766 million in 1997 and essentially unchanged from $1,467 million in 1996.

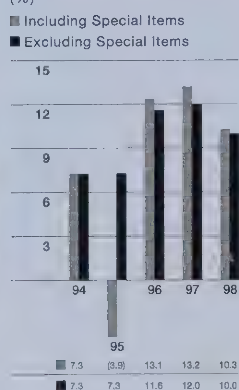
INCOME PER SHARE – CONTINUING OPERATIONS
($)



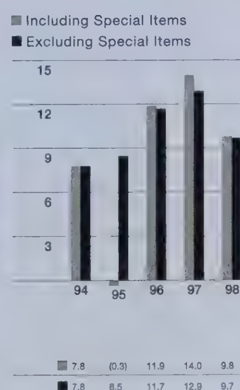
CONSOLIDATED OPERATING INCOME
($ millions)



RETURN ON AVERAGE SHAREHOLDERS' EQUITY – CONTINUING OPERATIONS
(%)



RETURN ON AVERAGE CAPITAL EMPLOYED
(%)



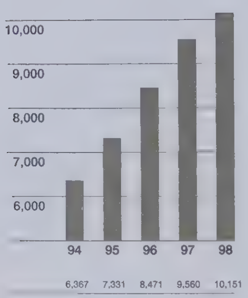
Income from discontinued operations was $309 million in 1997 and $29 million in 1996. In the third quarter of 1997, the Corporation sold its equity investment in Laidlaw for proceeds of $991 million and recognized an after-tax gain of $272 million. The gain and equity earnings from Laidlaw prior to its sale, as well as a net loss of $5 million incurred by Marathon Realty in 1996 prior to its sale, effective September 30 of that year, are included in income from discontinued operations.

Special items are detailed in the table on page 27. These included Canadian Pacific Railway's sale in 1998 of a marine freight operation and a partially offsetting provision for costs related to Year 2000 issues for a net gain of $15 million to operating income and $20 million to net income. The railway's non-core asset sales increased operating income by $134 million in 1997 and $17 million in 1996 and net income by $100 million in 1997 and $17 million in 1996. In 1996, net income from the railway was also increased by $103 million as a non-cash gain of $120 million from the repayment of Consolidated Debenture Stock was partially offset by an after-tax charge of $17 million related to restructuring accruals.

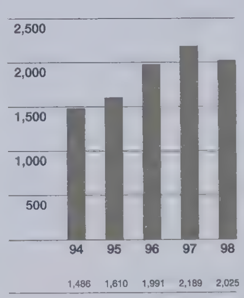
In 1997, Canadian Pacific Hotels surfaced value with the disposition of 11 business hotels to Legacy Hotels Real Estate Investment Trust (Legacy) and purchase of a one-third interest in Legacy. Gross proceeds on the sale were $887 million, while net proceeds of $642 million reflected the retention of Canadian Pacific Hotels' one-third equity interest. The after-tax gain was $100 million. In 1996, Canadian Pacific Hotels realized an after-tax gain of $20 million on sale of shares in Doubletree Hotels Corporation.

A partial offset to these gains were special corporate expense provisions of $113 million in 1997 and $47 million in 1996 on an after-tax basis, which included general tax provisions of $35 million and $25 million, respectively.

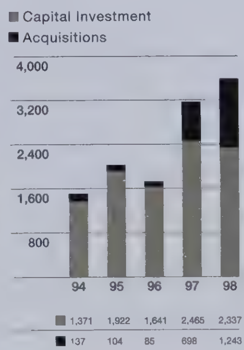
CONSOLIDATED REVENUES
($ millions)



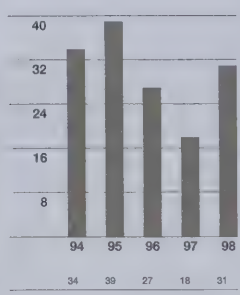
CASH FLOW
($ millions)



INVESTMENT SPENDING
($ millions)



NET DEBT AS A PERCENTAGE
OF NET DEBT AND EQUITY

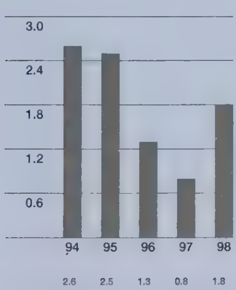


Special Items

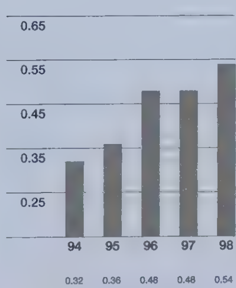
(in millions)	Operating Income	Non-Operating Income	Net Income
Effect on 1998:			
Gain on disposition of coastal marine freight operation	**$ 44**	**$ –**	**$ 36**
Canadian Pacific Railway's costs associated with Year 2000 issues	**(29)**	**–**	**(16)**
Total	**$ 15**	**$ –**	**$ 20**
Effect on 1997:			
Gain on disposition of Laidlaw Inc.*	$ –	$ –	$ 272
Gain on disposition of business hotels	–	211	100
Gain on disposition of Kansas City & Corn Lines	54	–	33
Gain on St. Lawrence & Hudson rationalization	42	–	29
Gain on Molson Centre lease monetization	38	–	38
Corporate provision – including $35 for general tax	–	(140)	(113)
Total	$ 134	$ 71	$ 359
Effect on 1996:			
Gain on repayment of Consolidated Debenture Stock	$ –	$ 120	$ 120
Gain on sale of Doubletree shares	–	31	20
Gain on sale of equity investment	17	–	17
Railway restructuring accrual discount amortization	–	(30)	(17)
Corporate provision – including $25 for general tax	–	(34)	(47)
Total	$ 17	$ 87	$ 93

** Gain on disposition of Laidlaw Inc. is included in discontinued operations.*

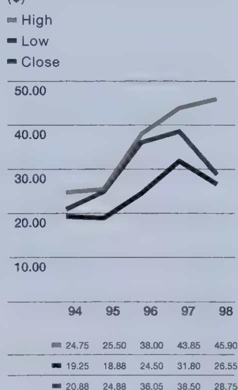
NET DEBT TO CASH FLOW



DIVIDENDS PER SHARE
($)



SHARE PRICE
($)



STRONG FINANCIAL POSITION

The Corporation's resilient cash flow and rich array of underlying assets provide a solid foundation from which to grow its businesses and improve the efficiency of its asset base even in tough business environments. Cash flow of $2,025 million in 1998 was a decrease of 8% from 1997 and an increase of 2% over 1996.

Surfacing value from the Corporation's wealth of assets funded a significant portion of its investing activities, with proceeds of $158 million in 1998, $2,305 million in 1997 and $807 million in 1996. The Corporation sold assets that were not contributing meaningfully to the bottom line, including its equity interest in Laidlaw and non-core rail lines, and also surfaced value with the formation of Legacy Hotels REIT and the monetization of a lease on the Molson Centre in Montreal.

The Corporation pursued profitable growth through investing activities that included significant strategic acquisitions, primarily beyond its Canadian base. During 1998, expenditures on acquisitions totalled $1,243 million, including $958 million at Canadian Pacific Hotels for Princess Hotels and Delta Hotels, and $285 million mainly at CP Ships for Ivaran Lines and ANZDL. In 1997, business acquisitions and investment spending was $698 million, consisting of $466 million at PanCanadian for CS Resources and $232 million mainly at CP Ships for Lykes Lines and Contship Containerlines.

Canadian Pacific also continued to build and strengthen its businesses with capital spending of $2,337 million in 1998, $2,465 million in 1997 and $1,641 million in 1996 for additions to equipment and plant assets.

The Corporation's management continues to stress the maximization of shareholder value with the efficient allocation of resources to promote growth within the businesses and increase returns to shareholders. In 1998, a strong financial position and cash flow supported an increase in the dividend, a continuation of the Common Share buy-back program begun in 1997, and continued investment in the businesses.

The quarterly dividend payable was raised to 14 cents per Common Share from 12 cents per share, effective with the dividend payable in July 1998.

The outlay for the share buy-back program was $325 million in 1998 and $272 million in 1997. The average number of shares outstanding in 1998 decreased to 335.8 million from 345.4 million in 1997 and 344.4 million in 1996. Under its share buy-back program, the Corporation purchased approximately nine million Common Shares in 1998 and seven million Common Shares in 1997.

The consolidated net borrowing position increased to $3,745 million at December 31, 1998 from $1,779 million at year-end 1997 and $2,589 million at year-end 1996, and the net debt-to-equity ratio remained low but moved up to 31:69 from 18:82 and 27:73, respectively. The net debt-to-equity ratio and the net debt-to-cash-flow ratio of 1.8:1 at December 31, 1998, both demonstrate Canadian Pacific's continued strong financial position.

SHARE PRICE

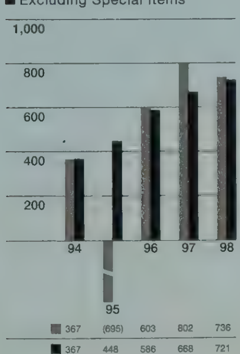
In 1998, turbulent financial markets and weak commodity markets hurt the Common Share price. The 1998 year-end closing price on The Toronto Stock Exchange was $28.75 down from $38.50 at year-end 1997. This followed a period of steady growth from $20.88 at year-end 1994.

CPR Core Network

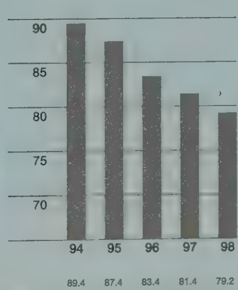
Operating Results by Business

started, in 1996, a four-year revitalization program designed to reduce costs and increase asset utilization. The program included re-engineering activities, rationalizing trackage and adopting new technology. The company also undertook an aggressive capital spending program designed to renew its franchise that was directed at locomotives, track and roadway, terminals and information systems. These initiatives resulted in greater cost-effectiveness and better service capability, which increasingly provided opportunities for greater market share and new areas for growth.

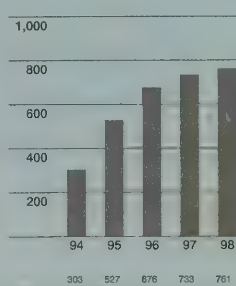
OPERATING INCOME
($ millions)
Including Special Items
Excluding Special Items



OPERATING RATIO
EXCLUDING SPECIAL ITEMS
(%)



CASH FLOW
($ millions)



Canadian Pacific Railway

IMPROVING PERFORMANCE AND INCREASING CUSTOMER SATISFACTION

Canadian Pacific Railway intensified its focus on improving product quality to reinforce and build its business. The upgrade of the road locomotive fleet, which will bring the average age down to approximately 15 years in 2001 from 23 years in 1995, supports product quality efforts. Purchases included 90 locomotives in 1997 and 120 in 1998, with 37 scheduled for delivery early in 1999 and another 16 in 2001. These new, advanced technology units help increase overall system train speed and improve reliability as well as reduce maintenance costs and fuel consumption. Track and facility enhancements increased capacity and improved train speed.

New efforts in 1998 to increase customer satisfaction included integrated account management teams, covering all aspects of customers' requirements, and enhanced partnerships with U.S. railroads to facilitate the flow of product. Furthermore, the railway continued its program to invest in state-of-the-art technology for its information systems with a special emphasis on the ability to allow for more timely, accurate and flexible product management and tracking, as well as better service reliability and increased asset utilization.

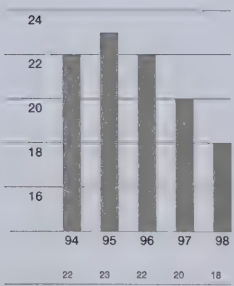
Canadian Pacific Railway

(in millions – excluding Special Items)	**1998**	1997	1996
Revenues	**$ 3,472**	$ 3,583	$ 3,543
Expenses	**2,751**	2,915	2,957
Operating income	**$ 721**	$ 668	$ 586
Operating ratio	**79.2%**	81.4%	83.4%

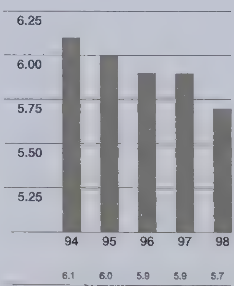
OPERATING INCOME

Operating income, excluding special items, increased to $721 million in 1998 from $668 million in 1997 and $586 million in 1996. Cost reductions were a significant factor in the improvement. 1998 was the first year in which the operating ratio fell below 80%, improving to 79.2% from 81.4% in 1997 and 83.4% in 1996.

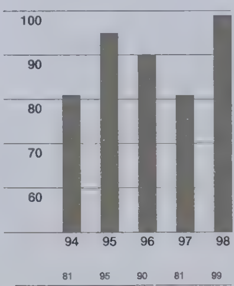
ROAD LOCOMOTIVE FLEET AGE
(years)



FUEL EFFICIENCY
(litres/1000 GTMs)



NON-BULK ON-TIME PERFORMANCE
(% within six hours)



In 1998, revenues from ongoing operations benefited from strong growth in intermodal business. This was offset by weak grain prices, the non-recurrence of the record grain crop of 1997 and the impact of weak Asian demand for some bulk commodities in 1998. Non-core asset sales bolstered results, providing gains of $44 million in 1998, $134 million in 1997 and $17 million in 1996.

Cash flow of $761 million in 1998 compared to $733 million in 1997 and $676 million in 1996. The return on average capital employed, excluding special items, rose to 11.3% in 1998 and 11.4% in 1997 from 11.1% in 1996.

REVENUES

Revenues from ongoing operations, excluding special gains on non-core asset sales, totalled $3,472 million in 1998 and were down from $3,583 million in 1997. Grain revenues were down as customers held back shipments in the face of weak prices, and difficult economic conditions in Asia depressed coal revenues. Declines in these commodities were partially offset by significant gains in intermodal, automotive and forest products. Revenues in 1997 were up $40 million from $3,543 million in 1996 as a record 1996/97 grain crop year combined with strong export potash volumes and higher Canadian coal exports to offset forgone business on the sale of the Kansas City & Corn Lines (KCCL). The KCCL revenues were $52 million in the period prior to its sale early in April 1997 and $217 million in 1996.

Overall, revenue-ton-miles (RTMs) were down 3% to 102.2 billion in 1998 and ahead 2% to 105.8 billion in 1997. Revenue per RTM of 3.24 cents in 1998 was unchanged from 1997, but down from 3.27 cents in 1996. Revenue per RTM is affected by pricing changes as well as variations in the traffic mix. Those for bulk traffic are generally lower than those for other products such as intermodal and automotive.

Revenues

(in millions)	1998	Changes Volume	Changes Price	1997	Changes Volume	Changes Price	1996
Freight revenues, excluding KCCL	$ 3,315	(168)	106	$ 3,377	220	(5)	$ 3,162
KCCL	–			52			217
Other revenues	201			288			180
	$ 3,516			$ 3,717			$ 3,559

Freight Revenues

(in millions)	1998	%	1997	1996	1995
Grain	$ 771	23	$ 845	$ 746	$ 769
Coal, sulphur and fertilizers	928	28	978	895	896
Forest products	353	11	317	320	340
Other resources	504	15	507	492	480
Intermodal	757	23	686	668	700
Automotive	269	8	252	233	246
Other*	(267)	(8)	(208)	(192)	(222)
Sub-total	3,315	100	3,377	3,162	3,209
KCCL	–	–	52	217	200
Total freight revenues	$ 3,315	100	$ 3,429	$ 3,379	$ 3,409

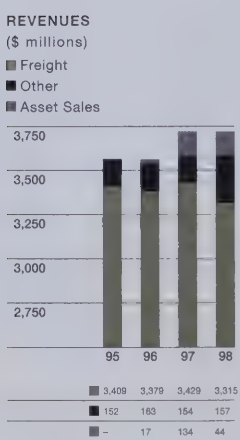
** Other includes claims and adjustments.*

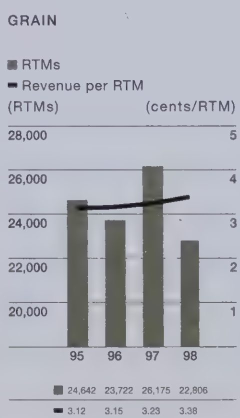
In the major commodity groups, grain revenue amounted to $771 million in 1998, $845 million in 1997 and $746 million in 1996. In Canada, the Canadian Transportation Agency allowed grain rate increases of 7% on August 1, 1996 and 2% on August 1, 1997, but a decrease of 1% on August 1, 1998. The revenue increase in 1997 and subsequent decrease in 1998 were largely attributable to the record Canadian grain crop of 1996/97 and depressed world prices in 1998. In the U.S., better service levels resulted in market gains in 1998. The railway is committed to improving service quality and increasing market share with a focus on having new high-throughput elevators built on its lines in Canada.

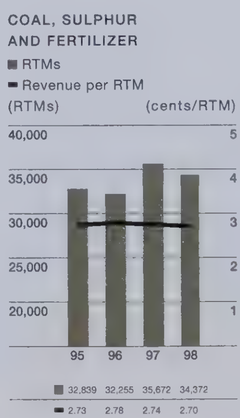
Coal, sulphur and fertilizer revenue decreased $50 million to $928 million in 1998 after an increase of $83 million to $978 million in 1997. After a period of growth, oversupply on world coal markets and competitive pressure from Australian producers put downward pressure on both rates and volumes in 1998. Coal revenues of $464 million in 1998 were down $61 million from 1997 and $34 million from 1996. Canadian Pacific Railway serves its sister company, Fording, Canada's leading metallurgical coal exporter and one of the railway's major customers. The companies are working together to realize new sales opportunities to mitigate the adverse impact of weak demand from Asian countries. Sulphur and fertilizer volumes remained strong in 1998 and 1997, due to healthy export markets.

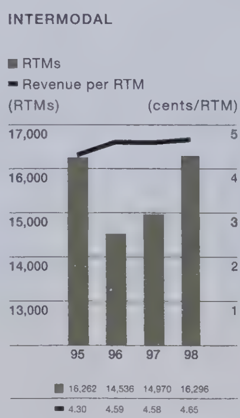
Forest products' revenues increased $36 million to $353 million in 1998 after a small decline of $3 million to $317 million in 1997. Other resource product revenues were virtually unchanged at $504 million in 1998 following an increase of $15 million to $507 million in 1997. The railway exited low-margin businesses in 1997 to concentrate on more profitable opportunities. It is now successfully growing these businesses, particularly forest products where the addition of new handling facilities and car fleet resulted in a significant boost to shipments in 1998.

Improved service, specialized product offerings and the expansion of terminal capacity, together with a stronger economy, led to intermodal revenue gains of $71 million, or 10%, to $757 million in 1998 and $18 million, or 3%, to $686 million in 1997. The segment was Canadian Pacific Railway's fastest growing business. The company continued to invest in the addition or expansion of key intermodal









terminals. The railway gained volumes at the Port of Montreal and the Port of Vancouver. It also benefited from more ocean carriers calling at the Port of Vancouver and its ability to run the shortest route between Vancouver and Chicago, North America's primary rail hub.

The railway experienced consecutive annual increases in automotive revenues, up $19 million to $252 million in 1997 and $17 million to $269 million in 1998. The railway captured new business, which necessitated some reduction in rates, and is focusing on adding inbound vehicle traffic at the Port of Vancouver.

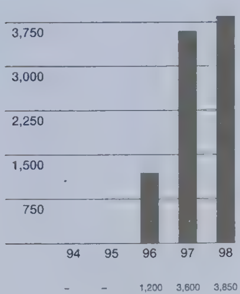
OPERATING EXPENSES

In late 1995, Canadian Pacific Railway announced an aggressive track rationalization program and head count reduction program designed to trim costs and enhance operating efficiency. At year-end 1998, some 3,850 miles, or 70% of the approximate 5,500 miles of the non-core rail lines had been divested, up from 3,600 miles at year-end 1997 and 1,200 miles at year-end 1996. As rationalization continues, average track density improves, infrastructure costs are reduced and funds are generated for reinvestment in the mainline track.

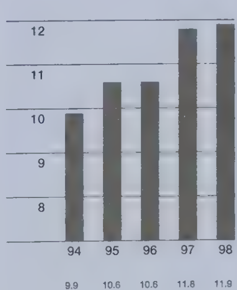
The average number of active employees was reduced to 19,860 in 1998 from 20,150 in 1997, 21,730 in 1996 and 23,420 in 1995. The resulting labour cost-saving was augmented by the adoption of more flexible work rules to increase labour productivity. Gain-sharing programs that align how key business functions are performed with the achievement of productivity and service goals have also strengthened productivity.

The upgrading of the locomotive fleet with advanced technology units was also an important contributor to cost savings. Lower maintenance requirements on the new locomotives resulted in reduced mechanical expenses and higher utilization. Transportation expenses benefited from lower fuel costs for the new locomotives, with estimated fuel efficiency savings of 20% for each locomotive. In addition, the replacement of leased locomotives by owned equipment contributed to significant cost savings.

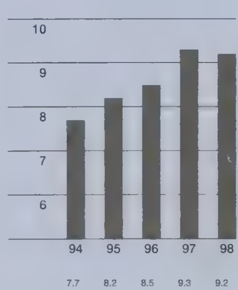
TRACK RATIONALIZATION
(cumulative track mileage divested since 1995)



GROSS TON MILES PER MILE OF ROAD OPERATED
(millions)



GROSS TON MILES PER ACTIVE EMPLOYEE
(millions)



The disposal of non-core network, reduced staffing, and the cost savings from the locomotive modernization program were the key drivers of the cost reductions. The rationalization of maintenance facilities and rework of procurement systems also contributed to good cost control. Operating expenses decreased $164 million to $2,751 million in 1998, after excluding a special expense of $29 million in 1998 for costs related to Year 2000 issues. The benefits of operating efficiencies and lower fuel prices were partially offset by the effects of shifts in traffic mix to an increased proportion of higher-cost intermodal freight – 23% of total 1998 freight revenues versus 20% in 1997. Operating expenses of $2,915 million in 1997 were down from $2,957 million in 1996, despite harsh winter conditions and higher traffic in 1997.

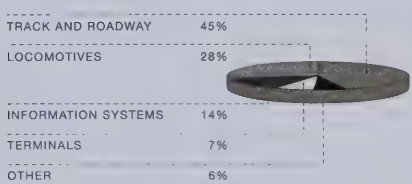
CAPITAL SPENDING

The disposition of non-core rail line assets improved efficiency and, together with the sale of other non-core assets, generated substantial sale proceeds which were reinvested with operating cash flow to finance the revitalization of the railway. Proceeds included $44 million on the sale of the west coast marine operations in 1998, and $465 million on the disposition of the KCCL, rationalization of the St. Lawrence & Hudson Railway and monetization of a lease in 1997.

Investment in 1998 and 1997 focused largely on renewing the track and roadway, as well as locomotive fleet, with advanced technology units that yield a hauling capacity almost twice that of the railway's standard road locomotives. Capital investment in 1998 and 1997 totalled $1,102 million and $858 million, respectively, and also included spending on terminals and information systems designed to make the railway highly competitive and more efficient.

A locomotive purchase program began in 1995 and included the acquisition of 346 AC-traction locomotives at a total cost of approximately $950 million. Deliveries to date included 83 units in 1995 at a cost of $217 million, 90 units in 1997 at a cost of $223 million and 120 units in 1998 at a cost of $331 million. 53 units will follow in 1999 and later years at a cost of about $180 million. These 346 units have hauling capacity equivalent to about 570 conventional, direct-current road locomotives.

1997-1998 CAPITAL INVESTMENT



The spending on track and roadway focused on two high-volume corridors – the export corridor between Calgary and Vancouver and the south corridor between Moose Jaw and Chicago. The railway continued work on new freight terminals that will increase container and trailer capacity. In 1998, construction was completed at a new facility in Calgary and at the Bensenville yard in Chicago. The U.S.$50 million investment at Bensenville nearly doubled capacity and introduced advanced control technology, supporting the company's position as a strong Canadian interline partner for U.S. railroads. A significant investment in information systems technology at Bensenville will help streamline business processes and provide new computer applications to support decision making. Projects intended to increase capacity and improve handling efficiencies were completed in 1998 at other facilities in Regina, Toronto and Minneapolis. Expansion of Canadian Pacific Railway's Montreal intermodal facility was started in 1998 and is scheduled for completion in the third quarter of 1999 and a new intermodal terminal at Vancouver should be completed in July 1999. The combined intermodal handling capacity at key locations – Montreal, Toronto, Calgary and Vancouver – will increase by 60%.

In 1998 and 1997, Canadian Pacific Railway invested some $276 million in the modernization of its computing and communications infrastructure. Over the next three years, the company expects to invest approximately $100 million to support an accelerated development of new systems that will improve productivity and customer service to become a leader in providing scheduled, reliable transportation.

Capital expenditures are expected to decline to some $800 million in 1999, the final year of the asset renewal program.

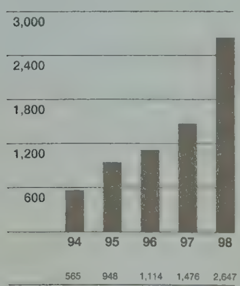
OUTLOOK

Canadian Pacific Railway has demonstrated success at improving operating performance and customer satisfaction. It will pursue market share gains and the development of new business opportunities. In particular, the company will look to develop opportunities in the U.S. Northeast based on the new access obtained after the acquisition of Conrail by CSX and Norfolk Southern.

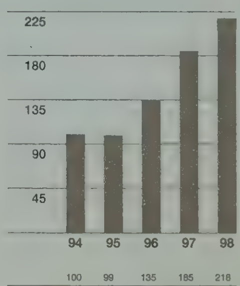
For 1999, Canadian Pacific Railway expects continuing softness in bulk commodity shipments, particularly coal and grain. However, the benefits of expense reductions, franchise renewal and improved service should help mitigate these factors. In addition, there should be further gains in non-bulk traffic if growth in the North American economy continues.

has increased its scale through acquisitions. In 1997, CP Ships expanded beyond the North Atlantic, where it operates Canada Maritime and Cast, with the purchase of Lykes Lines and Contship Containerlines. In 1998, CP Ships grew further with the purchase of Ivaran Lines and Australia-New Zealand Direct Line (ANZDL). Early in 1999, CP Ships formed a 50/50 joint venture with Transportación Marítima Mexicana (TMM). The joint venture includes Lykes Lines, Ivaran Lines and all the shipping line businesses of TMM. CP Ships now operates in three regional markets – North Atlantic, Australasia and Latin America – and is one of the ten largest shipping companies in the world, even though it does not directly compete in the world's largest Asia-Europe and Asia-U.S. trades.

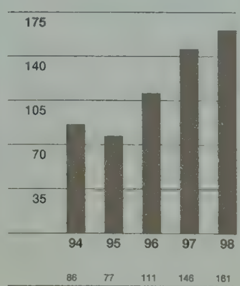
REVENUES
($ millions)



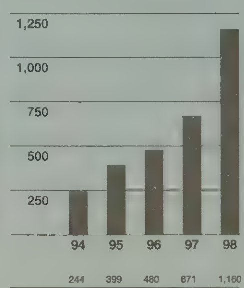
CASH FLOW
($ millions)



OPERATING INCOME
($ millions)



CONTAINER CARRYINGS
(thousand teus)



CP Ships

LEADER IN NORTH ATLANTIC TRADES

CP Ships is the Port of Montreal's largest carrier of containerized cargo and the leading container ship operator serving the trades between North America and Northern and Mediterranean Europe. CP Ships lowered the cost structure at its original businesses, Canada Maritime and Cast, through increased economies of scale, thereby strengthening their market positions. The 1997 acquisition of Lykes Lines, which offers services linking Europe to the U.S. East Coast and U.S. Gulf, and the U.S. Gulf to Africa, reinforced CP Ships' position in the transatlantic. The acquisition of Contship Containerlines in 1997 provided a platform from which to grow beyond the North Atlantic into new regional trades through its services connecting Europe with Australasia, the Indian Sub-Continent, the United States and South America.

EXPANSION INTO NEW TRADES

Building on this base, in May 1998, CP Ships acquired Ivaran Lines with services linking North America to Central and South America furthering CP Ships' goal to become a leader in Latin American trades.

In December 1998, CP Ships strengthened substantially its position in Australia-New Zealand trade with the acquisition of ANZDL, building on the platform provided by the acquisition of Contship Containerlines. ANZDL is a market leader in two key regional trades, U.S. West Coast to and from Australia and New Zealand and between Australia and New Zealand across the Tasman Sea.

In early 1999, CP Ships took another step toward becoming a Latin American regional market leader by forming the joint venture with TMM. The 50/50 joint venture, Americana Ships, brings together Lykes Lines, Ivaran Lines and TMM, providing substantial potential for service improvements and cost-saving synergies.

At the end of 1998, CP Ships consisted of six shipping lines, versus two at the end of 1996. Throughout, CP Ships has continued to operate on the same formula – to keep costs low and efficiency high by taking advantage of operational synergies. With each acquisition the scope for lowering costs and increasing efficiency grew. CP Ships also tries to provide the best customer service in terms of transit times and service frequency in each of its trade lanes.

In the past two years, CP Ships has not only reduced its exposure by diversifying beyond the North Atlantic, but it has also attained the stature and geographical reach of a world class container shipping business. This means that in their respective markets the CP Ships lines enjoy a special competitive edge because they operate with the resources and scale economies of a worldwide carrier, but with the flexibility and agility of the regional specialists that they are. CP Ships is one of the most profitable container shipping lines in the world.

CP Ships

(in millions)	**1998**	1997	1996
Revenues	**$ 2,647**	$ 1,476	$ 1,114
Expenses	**2,486**	1,330	1,003
Operating income	**$ 161**	$ 146	$ 111

OPERATING INCOME

Record operating income of $161 million was earned in 1998, up 10% on the previous record of $146 million in 1997, which in turn was 32% higher than the $111 million in 1996.

Despite increasingly difficult industry fundamentals, CP Ships' regional focus and cost drive have enabled it to perform well. However, freight rates, under pressure from excess industry capacity and global carriers' expansion, weakened in all trades, especially in 1998.

Although competition remains intense, the Montreal gateway carriers, Canada Maritime and Cast along with the Montreal Terminals business, managed to maintain volume, down only 1% in 1998 after an increase of 4% in 1997. They also succeeded in protecting margins, but only with the benefit of favourable exchange rates and lower unit costs. Their operating income contribution was down slightly from 1997, but still a strong improvement over 1996.

The growth in profits was also derived from the acquisition of new businesses. This increase in scale provided opportunities to enhance revenues with improved services throughout the group, as well as to realize synergies for expense savings.

The 1997 acquisitions – Lykes Lines and Contship Containerlines – made a substantial contribution in 1998 because of the reversal of operating losses at Lykes Lines and a full-year contribution from Contship Containerlines. The turnaround at Lykes was achieved by significant service improvements, the closure of a loss-making service, sharply lower costs and a revitalized organization. Contship Containerlines made steady progress achieving a better level of profits. Its problematical round-the-world service, following a schedule, partnership and tonnage reorganization, improved significantly in the second half of 1998.

Since its acquisition in the second quarter of 1998, Ivaran Lines incurred an operating loss. The South American trades suffer from falling volumes and serious overcapacity. A major rationalization program for all aspects of the business is underway and the management of Lykes Lines now runs it. ANZDL made a profitable contribution during the short period in which it was in the group.

Cash flow was up to $218 million in 1998 and $185 million in 1997, compared to $135 million in 1996. The return on average capital employed was strong at 21.7% in 1998, though down from 35.7% in 1997 and 45.2% in 1996.

REVENUES

CP Ships' revenues doubled with the acquisition of Lykes Lines, Contship Containerlines, Ivaran Lines and ANZDL. Revenues of $2,647 million in 1998 compared with $1,476 million in 1997 and $1,114 million in 1996. Average unit revenue in nearly all trade lanes was down due to competitive pressure. However, the group now has a higher proportion of long-haul trades with correspondingly higher absolute freight rate levels. Container carryings rose to over one million twenty-foot equivalent units (teus) in 1998 from 671,000 teus in 1997 and 480,000 teus in 1996.

Full year contributions from ANZDL and the new joint venture with TMM should add further revenue gains in 1999.

OPERATING EXPENSES

Operating expenses increased $1,156 million to $2,486 million in 1998 following an increase of $327 million to $1,330 million in 1997, largely as a result of the acquisitions made in 1997 and 1998. Offsets included lower fuel costs, favourable exchange rates and, importantly, the continuing drives to reduce costs and increase efficiency. The latter included the reconfiguration of service schedules, combined agency operations, as well as the integration of logistics operations across the group. This allowed for better utilization of containers and streamlined inland and terminal operations. In all of the lines, unit costs fell and the successful turnaround of Lykes Lines was an example of the significant impact of these efforts.

CAPITAL SPENDING

CP Ships took delivery of two additional containerships in each of 1997 – Canmar Valour and Canmar Reliance – and 1998 – Canmar Pride and Canmar Honour. These new ships reduced dependence on charters and improved route efficiency.

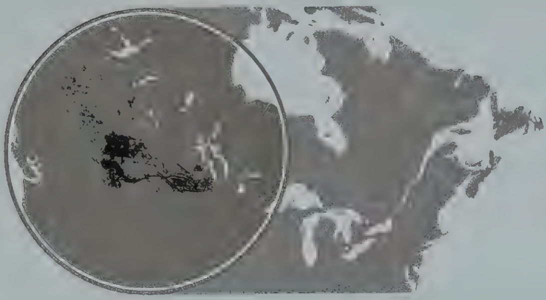
Additions to properties amounted to $125 million in 1998 and $89 million in 1997, mainly for containers, an additional second-hand ship and the upgrading of equipment at Montreal Terminals. As well, there was replacement and development investment in information systems.

CP Ships is well positioned to seize opportunities to strengthen market positions and further reduce costs by additional regional acquisitions or alliances that may materialize.

OUTLOOK

CP Ships' focus in 1999 is to extract full value from its recent acquisitions and joint venture, which have created an annual throughput of some 1.4 million teus, by improving service, integrating operations and driving down costs in the face of excess industry capacity and increased competition. Its regional, as opposed to global, emphasis should help it perform more profitably than many of its competitors. However, the falling freight rates experienced over the last two years, which became more apparent in the fourth quarter of 1998, are expected to continue through 1999.

Unless the economic difficulties in Asia worsen and have a more widespread effect, CP Ships should continue to be relatively unaffected by weak Asian demand.

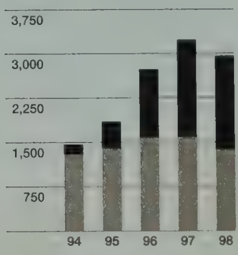


Western Canada Land Base

International Interests

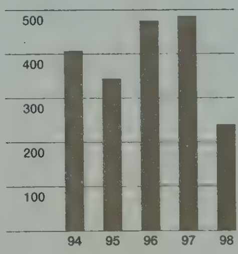
faced a difficult oil price environment in 1998. Early in the year it recognized the need to lower its cost structure and shift capital to higher return projects, primarily natural gas exploration and development. Operating expenses were reduced by 18% and the workforce was cut by 10%. Natural gas production increased 7% in response to a better price environment and the availability of expanded pipeline capacity.

REVENUES
($ millions)
Excluding Marketing Activities
Marketing Activities



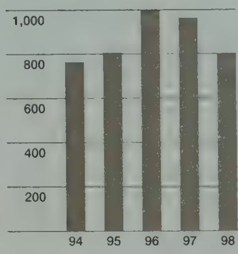
	94	95	96	97	98
Excluding Marketing Activities	1,316	1,412	1,599	1,610	1,392
Marketing Activities	162	446	1,145	1,629	1,574

OPERATING INCOME
($ millions)



94	95	96	97	98
407	344	475	485	236

CASH FLOW
($ millions)



94	95	96	97	98
763	805	1,001	961	802

PanCanadian Petroleum

CAPITAL EFFICIENCY

Early in 1998, PanCanadian restructured into business units, giving each the ability to manage its own unique set of challenges and opportunities. The business unit structure focuses management on identifying opportunities that maximize profitable production and minimize both finding and development costs and overhead costs. In particular, each unit is conducting an in-depth review of its portfolio of properties to identify the best opportunities and timing for development, farm-out, divestiture and/or acquisition. The new units are called: Palliser, Heavy Oil, South Central Alberta, Weyburn, East Coast, Selkirk, and Foothills and Frontier.

The Palliser unit produced 42% of total production, including 73% of gas production, and represented almost one-half of PanCanadian's reserves in 1998. The operations are principally on lands on which the company owns the mineral rights. The Heavy Oil unit provided 13% of total production and included 15% of proved reserves in 1998. The South Central Alberta unit – 30% of total production and 27% of proved reserves – encompasses five million acres of fee land, of which only 32% was developed. At the Weyburn unit – 7% of total production and 6% of proved reserves – there is a project which will use an advanced technology, carbon dioxide miscible flooding, to provide a major boost to recovery and production. The project requires a highly specialized expertise which will be fostered in the new business unit structure. The scheduled start-up date of December 1999 could be revised as discussions are taking place with the carbon dioxide supplier that is re-examining its commitments.

The Selkirk unit as well as the Foothills and Frontier unit are primarily involved in exploration activities in North America. These include the Scotian Shelf offshore Nova Scotia, western Newfoundland, the foothills of Western Canada and the Gulf of Mexico where PanCanadian is seeking to develop profitable growth in new core areas.

A heightened focus on capital efficiency builds on PanCanadian's traditional strengths. It has a large, high-quality, fee land base in Western Canada that is relatively unexploited. Its largest source of production and revenue, an extensive block of land in Southeast Alberta, has a low cost structure. In addition, it has developed leading-edge technology in many aspects of its business which minimizes finding and development costs.

PanCanadian Petroleum

(in millions)	**1998**	1997	1996
Revenues	**$ 2,966**	$ 3,239	$ 2,744
Expenses	**2,730**	2,754	2,269
Operating income	**$ 236**	$ 485	$ 475

OPERATING INCOME

PanCanadian's results in 1998 and 1997 were adversely affected by the prolonged impact of a significant drop in realized oil prices – down 34% in 1998 after a decline of 13% in 1997. Its cash flow decreased 17% to $802 million after a smaller decrease of 4% to $961 million in 1997. The decline in cash flow was not as sharp as the decrease in operating income because of the high non-cash charges for depreciation and depletion.

PanCanadian's contribution to consolidated operating income was $236 million in 1998, down from $485 million in 1997 and $475 million in 1996. While oil prices were off sharply in 1998, there was a smaller decline in 1997 and the effects in 1997 were mitigated by stronger natural gas prices. The return on average capital employed was 4.7% in 1998, down from 11.0% in 1997 and 12.0% in 1996.

REVENUES

Total revenues decreased $273 million to $2,966 million in 1998, mainly because lower oil prices brought about a $239 million decline in revenues from crude oil, natural gas and natural gas liquids. In 1997, total revenues increased $495 million to $3,239 million, chiefly due to a $484 million increase in revenues from marketing third-party production. 1997 revenues from crude oil, natural gas and natural gas liquids were up $54 million to $1,585 million on stronger realized gas prices. In addition, revenues from CS Resources were included in results, effective with its acquisition on July 15, 1997.

Crown royalties and similar payments decreased to $100 million in 1998 from $142 million in 1997 and $160 million in 1996, mainly because of the lower oil prices, and helped offset some of the pressure on revenues.

Revenues		Changes			Changes		
(in millions)	**1998**	Volume*	Price	1997	Volume*	Price	1996
Crude oil	**$ 706**	10	(242)	$ 938	(49)	(83)	$ 1,070
Natural gas	**578**	39	(9)	548	3	176	369
Natural gas liquids	**62**	(5)	(32)	99	(3)	10	92
	1,346	44	(283)	1,585	(49)	103	1,531
Empress	**87**			112			105
Other	**59**			55			123
Royalties	**(100)**			(142)			(160)
	1,392			1,610			1,599
Marketing	**1,574**			1,629			1,145
Total revenues	**$ 2,966**			$ 3,239			$ 2,744

** Volume figures represent revenue variances resulting from production.*

CRUDE OIL REVENUES

Crude oil revenues before Crown royalties and similar payments amounted to $706 million in 1998, $938 million in 1997 and $1,070 million in 1996. Commodity and foreign exchange hedging activities for this operation resulted in a gain of $56 million in 1998 which contrasted with losses of $42 million and $119 million in 1997 and 1996, respectively. The gain in 1998 resulted mainly from commodity hedges.

The average realized price, excluding hedging, on PanCanadian's crude oil was down 34% to $13.91 per barrel in 1998 following a decline of 13% to $21.17 per barrel in 1997. The declines were chiefly attributable to the deterioration in world oil prices. Benchmark West Texas Intermediate (WTI) crude oil prices averaged U.S.$14.40 per barrel in 1998, down 30% from $20.61 U.S. per barrel in 1997 and down 35% from U.S.$22.01 per barrel in 1996. An increased proportion of heavy oil in the product mix, combined with a higher discount on the price of heavy crude versus light crude oil in 1998 and 1997, also contributed to lowering the average realized price. Measured by the Lloyd Blend heavy oil price, the differential averaged U.S.$5.52 per barrel in 1998, U.S.$6.55 per barrel in 1997 and U.S.$4.89 per barrel in 1996.

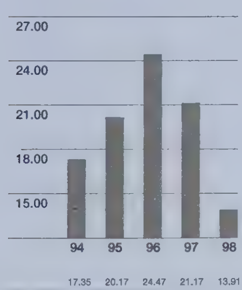
Crude oil production remained relatively flat. Volumes averaged 128,000 barrels per day in 1998, 127,000 barrels per day in 1997 and 133,000 barrels per day in 1996. The relatively flat production in 1998 was primarily the result of the shut-in of uneconomic oil volumes, given the poor price environment. In 1997, production shutdowns offshore Nova Scotia, the sale of non-core assets, and operational difficulties in heavy oil offset incremental production from the acquisition of CS Resources and an additional interest in the Weyburn field.

The price of WTI crude oil has exhibited limited potential for recovery. Oversupply conditions persist and the outlook for soft demand continues. A positive development is the narrowing of the price differential between light and heavy crude oil, though prices still remain depressed. Oil production will continue to be curtailed as long as these market conditions persist.

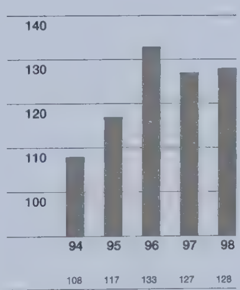
NATURAL GAS REVENUES

Growing natural gas production, coupled with better gas prices, provided an offset to sharply lower oil prices. Revenues from natural gas of $578 million in 1998, before Crown royalties and similar payments, were up $30 million from 1997 and $209 million from 1996. Included in results were a loss of $21 million in 1998, a gain of $21 million in 1997 and a loss of $50 million in 1996 from hedging activities. Currency hedges were the principal hedging activities in 1998 and 1997.

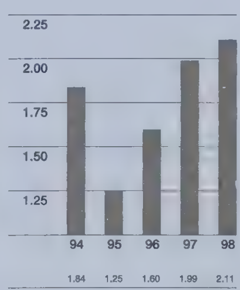
OIL PRICE
($ per barrel)



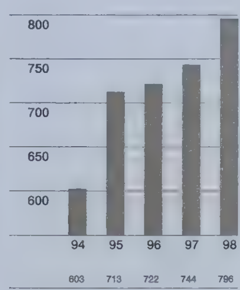
CRUDE OIL PRODUCTION
(thousand barrels per day)



GAS PRICE
($ per thousand cubic feet)



NATURAL GAS PRODUCTION
(mmcf per day)



PanCanadian received an average selling price, excluding hedging activities, for natural gas of $2.11 per thousand cubic feet in 1998, up from $1.99 in 1997 and $1.60 in 1996. There were reduced transportation charges in 1998 because PanCanadian negotiated a lower toll for product carried on the NOVA pipeline system, effective January 1, 1998. Daily production averaged 796 million cubic feet in 1998, ahead of 744 million cubic feet in 1997 and 722 million cubic feet in 1996. The production gains were made despite the sale in 1997 of a non-core property, which contributed 22 million cubic feet per day.

Natural gas prices remained strong throughout most of 1998. However, as the 1998/99 winter started off warm, there was some concern over continuing support for the price. PanCanadian has fixed the sales price on 468 million cubic feet per day of its natural gas production at a field gate price of $2.51 per thousand cubic feet for the calendar year 1999, with 95% of the fixed-price volumes occurring over the first ten months of the year.

OTHER ACTIVITIES

The volume of field natural gas liquids (NGL) is related to production of natural gas, its composition and the efficiency of recovery. Average daily production of NGL was some 13,000 barrels in 1998 and 1997, and 14,000 barrels in 1996. The decline in 1998 and 1997 was due to the disposition of interests in properties. The average realized prices per barrel were $13.61, $20.58, and $18.08 in 1998, 1997 and 1996, respectively. The revenue contribution decreased to $62 million in 1998 from $99 million in 1997 and $92 million in 1996.

PanCanadian has ownership interests in four NGL extraction plants that straddle two major gas transmission pipelines at Empress, Alberta. Revenues from PanCanadian's interests in these facilities were down to $87 million in 1998 from $112 million in 1997 and $105 million in 1996. Production of 13,000 barrels per day in 1998 was up slightly from each of the prior years, but product prices deteriorated in 1998 after some strengthening in 1997. In addition, higher feedstock costs put downward pressure on margins in both years. The gross operating margin decreased $26 million to $21 million in 1998 after a decrease of $5 million to $47 million in 1997.

PanCanadian's marketing revenues include third-party crude oil, natural gas and NGL marketed through several partnerships and joint venture agreements. Marketing revenues were $1,574 million in 1998, $1,629 million in 1997 and $1,145 million in 1996. After a period of expansion, revenues declined 3% in 1998 because of a reduction in third-party natural gas volumes and lower natural gas liquids prices. The gross margin on these activities was $39 million in 1998, $27 million in 1997 and $47 million in 1996. Margins on natural gas marketing improved in 1998 after intense market competition led to significantly tighter margins in 1997.

In March, PanCanadian consolidated the operations of its Calgary-based natural gas marketing group with its wholly-owned, U.S.-based marketing arm, National Gas & Electric, to form PanCanadian Energy Services. The new business unit, with headquarters in Houston, markets 1.8 billion cubic feet of gas per day.

In 1996, PanCanadian sold its 10% interest in Syncrude. Other revenues in 1996 included a contribution of $74 million from Syncrude in the period prior to its sale.

OPERATING EXPENSES

To alleviate the effects of persistently low oil prices, PanCanadian has been emphasizing operating cost improvements. Operating expenses associated with the working interest production of crude oil and natural gas were reduced by 18% to $5.05 for each barrel of oil equivalent in 1998 from $6.13 per barrel of oil equivalent in 1997. (Oil equivalent volumes are converted at a rate of 10,000 cubic feet of natural gas to one barrel of oil.) There was a 20% increase in 1997, primarily as a result of significantly higher costs associated with heavy oil wells and difficult first-half weather conditions. Operating expenses of $393 million in 1998 were down $62 million from 1997 and essentially unchanged from 1996.

In 1998, administrative expenses were up primarily as a result of a reduction in capitalized administrative expenses and costs associated with a 10% reduction in the workforce early in 1998. In 1997, the company incurred costs related to the purchase of CS Resources. Per barrel of oil equivalent, administrative expenses associated with oil and gas operating activities averaged $0.80 in 1998, $0.67 in 1997 and $0.50 in 1996.

The rate of depletion, depreciation and amortization, excluding reclamation, for Canadian exploration and development was $7.64 per barrel of oil equivalent in 1998, and $7.17 per barrel of oil equivalent in 1997 versus $6.70 per barrel of oil equivalent in 1996. The increases in 1998 and 1997 principally stemmed from the higher costs associated with finding and developing new reserves in Western Canada. In addition, the depletion, depreciation and amortization expenses of $637 million in 1998, $553 million in 1997 and $611 million in 1996 reflected three factors. In 1998, there was a reclamation provision for the company's East Coast offshore operations, and an increase in the depreciation rate for computer-related assets; in 1996, there was a writedown of $70 million, $58 million after tax, on international operations.

Excluding purchased product expenses and cost of sales at the Empress plants, operating expenses of $1,123 million in 1998 were up 4% from $1,082 million in 1997 and up 6% from $1,058 million in 1996.

Operating Expenses

(in millions)	**1998**	1997	1996
Cost of sales	**$ 393**	$ 455	$ 388
Administration	**93**	74	59
Depreciation and amortization	**205**	176	185
Depletion	**432**	377	426
	1,123	1,082	1,058
Empress	**57**	57	49
Purchased product	**1,535**	1,602	1,098
Other (includes goodwill amortization)	**15**	13	64
Total operating expenses	**$ 2,730**	$ 2,754	$ 2,269

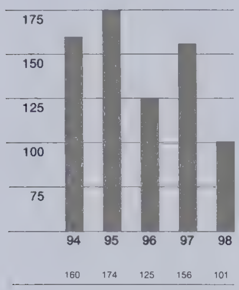
CAPITAL SPENDING

Over the past three years, PanCanadian's capital expenditures were mainly devoted to the exploration and development of crude oil and natural gas in Western Canada. In 1998, the company started to put particular emphasis on gas. Capital expenditures were reduced to $894 million in 1998 from the 1997 level of $1,245 million, excluding CS Resources which was acquired for $466 million. Spending in 1996 was $776 million, before the sale of PanCanadian's interest in Syncrude for $385 million.

Proved reserve additions included 81 million barrels of oil equivalent in 1998, excluding an adjustment to heavy oil reserves, 122 million barrels of oil equivalent in 1997 and 100 million barrels of oil equivalent in 1996. These results represented reserve replacement rates of 101% in 1998, 156% in 1997 and 125% in 1996. The finding and development costs associated with these additions were $10.12 in 1998, $8.75 in 1997 and $6.65 in 1996, per barrel of oil equivalent, with costs associated with activities in Western Canada of $7.93 in 1998, $7.67 in 1997 and $6.13 in 1996.

In light of the current economic environment, 31 million barrels of heavy oil reserves were removed from the proven category. Including this adjustment raises the 1998 finding and development costs, on a barrel of oil equivalent basis, to $16.47 per barrel on a consolidated basis and $12.74 per barrel in Western Canada.

PROVED RESERVES REPLACEMENT AS A PERCENTAGE OF PRODUCTION
(before acquisitions and dispositions and heavy oil adjustment in 1998 – BOE)



PanCanadian's large and diverse base of land holdings in Western Canada allows it to shift its focus to respond to opportunities in the marketplace. PanCanadian is emphasizing the development of its natural gas prospects to reduce the impact of the price and supply volatility of oil. In particular, PanCanadian's gas activities enjoy important advantages at the Palliser unit, including low-risk, shallow reservoirs with low associated finding and development costs, substantial existing infrastructure to support development, and access to low-cost pipeline transportation to market made possible by recent load retention rate agreements.

Increasingly the maturing Western Canadian basin has exhibited low productivity rates, higher expense and investment to maintain production rates, and shrinking reserves, especially for lighter oil. As a result, PanCanadian has taken a measured approach to broadening its search for new production sources on Canada's East Coast and in the Gulf of Mexico. The discovery in June 1998 on the Llano prospect in the Gulf of Mexico provides significant promise. This discovery has the potential to add 20,000 to 30,000 barrels per day of production to the company's sales over the next five years with production possible in early 2000. Furthermore, there are a number of other prospects in the immediate vicinity on blocks in which PanCanadian holds an interest.

International exploration plays accounted for approximately 14% of PanCanadian's capital expenditures in 1998 and 1997. The company also has interests in the United Kingdom, Australia, Africa and Venezuela.

PanCanadian will conduct regular, ongoing assessments of its oil and gas portfolio to ensure that development efforts and capital are directed towards the most rewarding opportunities first. In order to maximize returns, exploration and development efforts concentrate on areas where it is possible to leverage existing field infrastructure and transportation cost advantages.

PanCanadian's planned capital program for 1999 is down to approximately $650 million, reflecting the deferral of crude oil-related expenditures in response to the prevailing weak prices for this commodity. The majority of the spending in 1999 will be targeted to natural gas activities in Western Canada given the expected attractive economic returns.

OUTLOOK

In the face of weak crude oil prices, PanCanadian is focusing on reducing its operating costs and growing opportunities for profitable production. Its strong asset base bodes well for improved earnings when commodity prices improve. The current outlook is for increasing natural gas production, slightly higher oil prices and a narrowing of price differentials between heavy and light oil. The gas hedging currently in place should also support higher realized gas prices in 1999.

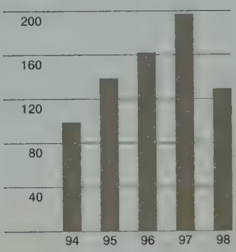
Operations

Diverse Export Coal Markets

is the largest, lowest-cost, metallurgical coal exporter in Canada and derives most of its revenue from the mining and processing of metallurgical coal in southeastern British Columbia. After several years of strengthening prices and increased sales to a broader customer base, decreased demand from Asia and oversupply of metallurgical and thermal coals hurt the performance of the export coal operation. Selling prices and sales volumes declined in 1998. To offset these pressures, Fording is directing its efforts towards further diversifying its sales markets and enhancing its low-cost producer status.

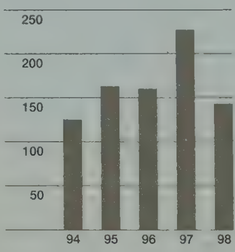
Fording is the largest producer of wollastonite in the world and its industrial minerals operations derive most of their revenues and operating income from this product.

OPERATING INCOME
($ millions)



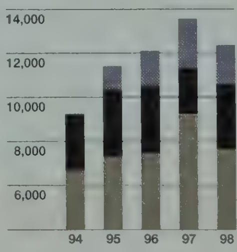
94	95	96	97	98
99	139	162	197	129

CASH FLOW
($ millions)



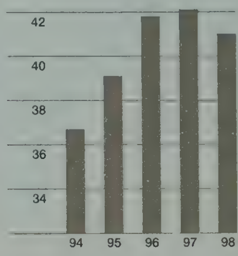
94	95	96	97	98
125	163	160	227	143

SALES VOLUME
AT B.C. MINES
(thousand tonnes)
Fording River
Greenhills
Coal Mountain



	94	95	96	97	98
Fording River	6,703	7,327	7,502	7,916	7,676
Greenhills	2,507	3,025	3,028	3,421	2,926
Coal Mountain	21	1,050	1,559	2,203	1,757

PRODUCTIVITY – TONNES
OF CLEANED COAL
(per employee per 8-hour shift)



94	95	96	97	98
36.7	39.1	41.8	42.1	41.0

Fording

Fording

(in millions)	1998	1997	1996
Revenues	$ 906	$ 1,018	$ 915
Expenses	777	821	753
Operating income	$ 129	$ 197	$ 162

OPERATING INCOME

Fording's operating income declined 35% to $129 million in 1998 from a record $197 million in 1997. The decline was principally due to the difficult export coal industry conditions. Contracts with the Japanese steel mills for the year starting April 1, 1998 provided for price reductions of up to 8%. In addition, volumes purchased under contract declined. Spot sales volumes and prices also deteriorated significantly. 1997 operating results were a $35 million, or 22%, improvement over 1996, chiefly reflecting increased coal sales volumes.

Cash flow of $143 million in 1998 compared with $227 million in 1997 and $160 million in 1996. The return on average capital employed declined to 12.2% in 1998 after averaging over 21% in 1997 and 1996.

REVENUES AND OPERATING EXPENSES

Revenues were $906 million in 1998, down from $1,018 million in 1997 but essentially unchanged from $915 million in 1996. Weak export coal markets in 1998 reversed the volume and price gains of 1997.

Operating expenses totalled $777 million in 1998, down $44 million from 1997 and up $24 million from 1996. These variances largely reflect the variations in the sales of export coal. The operating expenses of Minera NYCO, the new wollastonite operation in Mexico, were included for the first time in 1998.

Revenues

		Changes			Changes		
(in millions)	1998	Volume*	Price	1997	Volume*	Price	1996
Export coal operations	$ 769	(73)	(37)	$ 879	87	13	$ 779
Prairie operations	83			85			86
Industrial minerals operations	54			54			50
	$ 906			$ 1,018			$ 915

* *Volume figures represent revenue variances resulting from production.*

EXPORT COAL OPERATIONS

Operating income from the export coal mines in British Columbia was $86 million in 1998, $142 million in 1997 and $110 million in 1996. In 1998, operating income decreased 39% as sales volume declined 9% and the realized price net of transportation costs was down 3%. Operating income increased 29% in 1997, principally reflecting a 12% increase in export coal volumes.

Revenues from the mines in British Columbia amounted to $769 million in 1998, $879 million in 1997 and $779 million in 1996. Sales volume of cleaned coal of 12.4 million tonnes in 1998 decreased 8% from 13.5 million tonnes in 1997, after an increase of 12% over 12.1 million tonnes in 1996. Exports to Europe, the Mediterranean and Americas accounted for 49% of the sales volume in 1998, up from 44% in 1996 and 23% in 1993.

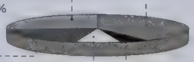
Metallurgical coal producers annually negotiate supply contracts with the Japanese steel industry. The U.S. dollar denominated prices are benchmarks for other sales throughout the world. For the coal year starting April 1, 1998, the Japanese benchmark pricing was adjusted downwards by 5% for higher quality coal and 8% for lower grades. The price decrease in 1998 followed two consecutive increases – 4% for the 1997 coal year and 12% for the 1996 coal year. The pressure on prices in 1998 was partially alleviated by lower transportation costs as rail rates were reduced to reflect the lower market price. The weakening of the Canadian dollar relative to the U.S. dollar did not provide an offset to U.S. dollar price declines. Fording had previously hedged a significant portion of its exposure to the U.S. dollar which resulted in an average rate on its sales of U.S.71.2 cents.

In December 1998, Fording concluded its price negotiations with the Japanese steel mills for the contract price of metallurgical coal from April 1, 1999 to March 31, 2000. The settlement resulted in a price reduction of approximately 18% for higher quality coal from an average of U.S.$50.45 per tonne to U.S.$41.45 on volumes similar to those delivered in 1998. Negotiations for lower quality coals are ongoing with the expectation of a similar percentage price reduction and quantities approximating 1998 levels.

Operating expenses at the export coal mines of $682 million in 1998 compared with $737 million in 1997 and $669 million in 1996. The decline in 1998 stemmed primarily from the reduced sales volume. The resulting lower utilization of production capacity brought the cost per tonne of cleaned coal produced up 6%, but many earlier years of productivity improvements held the unit cost in 1998 to a 5% increase in the past five years. Unit operating expenses in 1998 were adversely affected by increased depreciation charges from capital expenditures in 1997 to upgrade the plants and the truck and shovel fleets, as well as higher mineral tax payments. Operating expenses were up 10% in 1997 over 1996 as an increased volume and higher strip ratio (the ratio of waste moved to coal extracted) were only partially offset by a 3% reduction in the unit cost of clean coal sold.

METALLURGICAL COAL SHIPMENTS BY AREA

EUROPE/MEDITERRANEAN	41%
JAPAN	27%
KOREA	19%
AMERICAS	8%
TAIWAN	5%



INDUSTRIAL MINERALS OPERATIONS

The industrial minerals operations' operating income was down 50% to $9 million in 1998 after a small increase to $18 million in 1997. The deterioration in 1998 stemmed chiefly from losses during start-up of the new wollastonite mining and processing facility in Mexico.

Sales revenue from Fording's wollastonite operation in New York State and the new facility in Mexico was $54 million in 1998. Revenue in 1997 and 1996 from the operation in New York State was $54 million and $50 million, respectively. Sales volume of about 110,000 tonnes in 1998 was up 10% from the prior year and 16% from 1996. The average sales price in 1998 declined by 7% from 1997 levels and 16% from 1996 due primarily to a change in product mix and to a lesser extent competitive price pressures.

The sales volume at the new mine in Mexico, opened in 1998, was significantly below expectations because of an extended plant commissioning and a slower-than-expected market acceptance of the product. The Mexican operation is designed to produce and process large quantities of wollastonite and economies of scale are expected to lower its processing costs, keeping it competitive in the lower-priced market segment.

The U.S. operation in Willsboro, New York will focus on high-end product, which will be directed primarily to higher-margin applications. There was no change in sales volume at this operation in 1998.

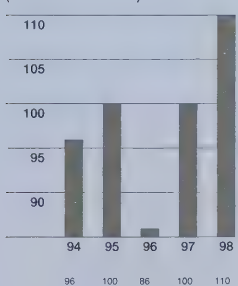
Operating expenses at the wollastonite operations amounted to $45 million in 1998, up 36% from $36 million in 1997 as a result of higher volumes and the start-up of the new mine in Mexico. Operating expenses were $36 million in 1996.

PRAIRIE OPERATIONS

Fording also earns operating income on mining and contract activities in Alberta and royalties on its properties throughout the Prairie Provinces. An important and stable source of earnings, these interests provided operating income of $34 million in 1998 and $37 million in both 1997 and 1996.

Fording continues to evaluate opportunities for development of its extensive coal resources as well as its mining expertise, including that developed from its participation in oil-sand mining at the Syncrude operation in Alberta.

SALES VOLUME OF WOLLASTONITE
(thousand tonnes)



CAPITAL SPENDING

Additions to properties declined substantially to $69 million in 1998 from $223 million in 1997 and $160 million in 1996. Completion of major projects was the main reason for the decrease in 1998. The new plant in Mexico, completed early in 1998, was built at a cost of $170 million over a three-year period. The upgrading of the British Columbia mines, especially Coal Mountain acquired in 1994 and modernized through 1998, entailed an outlay of some $120 million in the past three years. Capital expenditures are expected to be held at a lower level as major expansion projects have been completed. Fording will continue to invest in new technologies and equipment to improve production efficiency and product quality.

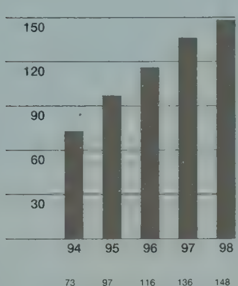
OUTLOOK

Fording's export coal operations enjoy a low-cost operating structure and good track record of productivity improvements. Fording will continue aggressive marketing and sales market diversification efforts, supported by its high quality product offering and blending capabilities to meet customer specifications. However, the metallurgical coal market has moved into oversupply due to the combined effects of increasing production, particularly from Australia, and a softening demand as steel consumption has fallen with Asia's economic downturn. Consequently, the near term outlook for export coal is difficult as reflected by the 18% price reduction negotiated with the Japanese steel mills for the 1999 coal year.

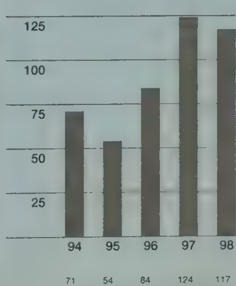
Efforts are being intensified in penetrating and developing markets for wollastonite products from the operations in New York and Mexico.

[illegible] has for many years held a unique position in Canada with broad geographic coverage through leading four-star business and resort hotels, most of which are landmark properties and enjoy strong name recognition. Canadian Pacific Hotels' strategy is to maximize profitability by offering superior customer service, enhancing its product offering with the addition of such services as spas and convention centres, expanding at existing properties and adding complementary properties. Canadian Pacific Hotels is also pursuing strategic acquisitions to strengthen its base business in Canada and expand its operations outside of Canada.

OPERATING INCOME
($ millions)



CASH FLOW
($ millions)



Canadian Pacific Hotels

GROWING THE CANADIAN BASE

In May 1998, Canadian Pacific Hotels acquired Delta Hotels which had annual revenues of $350 million in 1997 and which managed or franchised 34 properties with approximately 10,000 rooms. Canadian Pacific Hotels acquired the management company and the brand, as well as leasehold interests in three properties for $93 million. With Delta Hotels managed as a distinct brand, the acquisition provides Canadian Pacific Hotels with a solid entry into the higher-end, mid-market segment. In addition to providing a new product range, the purchase doubled Canadian Pacific Hotels' size in Canada, ensuring a continued leadership role in the Canadian industry and providing significant opportunities for synergies in support services. The acquisition also extends the opportunity to add management contracts, both nationally and internationally, that would perform well under the Delta Hotels flag. Since the acquisition, one of three leasehold interests has been purchased by Legacy Hotels Real Estate Investment Trust (Legacy).

In February 1998, Canadian Pacific Hotels also added two Toronto-area properties to its portfolio, providing a presence outside of the city's downtown core. The 368-room Toronto East property was repositioned as a Canadian Pacific hotel, and the 296-room Four Points property continued to carry the Four Points brand under a franchise agreement with Sheraton. Canadian Pacific Hotels also acquired an equity interest in and assumed the management contract for the Manoir Richelieu, a resort-style hotel in Charlevoix, Quebec. Substantial progress was made on the construction of Vancouver Airport Place, a $65 million luxury hotel located adjacent to the new terminal at the Vancouver International Airport. The 400-room property, which will be owned and managed by Canadian Pacific Hotels, is expected to open in the fall of 1999.

A NEW INTERNATIONAL PRESENCE

In August 1998, Canadian Pacific Hotels purchased for $865 million, Princess Hotels, which operates seven luxury resort properties, with over 3,000 rooms, in the United States, Bermuda, Barbados and Mexico. Its resort properties fit well with Canadian Pacific Hotels' prestige resort properties and add a warm-weather dimension and geographical diversification. There are opportunities for cost savings and improvement in revenue management. Together the hotels should also benefit from enhanced sales and marketing presence. The acquisition positions Canadian Pacific Hotels as the fourth largest, premier resort hotel operator in North America and the Caribbean and will serve as a platform for further growth.

SURFACING VALUE – LEGACY HOTELS REIT

In November 1997, Canadian Pacific Hotels surfaced significant value, net proceeds of $642 million, with the disposition of 11 business hotels to, and buying a one-third interest in, Legacy. Through management contracts, Canadian Pacific Hotels and Delta Hotels operate the Legacy properties. Additionally, the company receives incentive and advisory fees, as well as returns on its investment in Legacy.

Canadian Pacific Hotels

(in millions)	**1998**	1997	1996
Revenues	**$ 519**	$ 565	$ 566
Expenses	**371**	429	450
Operating income	**$ 148**	$ 136	$ 116

OPERATING INCOME

Canadian Pacific Hotels benefited from a strong domestic economy, a weak Canadian dollar and increasing international tourism. Growth through acquisitions was also an important contributing factor in 1998. A record operating income of $148 million in 1998 was up from $136 million in 1997, despite earnings forgone as a result of the sale of a partial interest in the business hotels in 1997. The 1997 operating income was a 17% improvement over 1996.

Cash flow generated was $117 million in 1998 and compared to $124 million in 1997 and $84 million in 1996. The return on average capital employed was 13.5% in 1998, 17.1% in 1997 and 11.6% in 1996.

REVENUES

Revenues under management grew to $1,241 million in 1998 from $741 million in 1997 and $661 million in 1996. Consolidated revenues of $519 million in 1998 compared with $565 million in 1997 and $566 million in 1996. The revenue decline in 1998 and flat revenues in 1997 reflected the sale of a partial interest in the business hotels, which continue to be managed by Canadian Pacific Hotels. The acquisition of Princess Hotels and Delta Hotels added revenues of some $113 million and $34 million, respectively, in 1998.

The Canadian resort properties experienced higher revenue per available room (RevPAR), ahead 10% to $138.73 in 1998 following an increase of 9% to $126.67 in 1997. This was led by better average room rates, up to $185.22 in 1998 and $173.29 in 1997 from $160.65 in 1996. The weakness in the Asian economies did not have a significant impact on the business, as the weak Canadian dollar resulted in increased demand from the U.S., European and domestic markets. Operating income from the Canadian resort properties was $86 million in 1998, $80 million in 1997 and $75 million in 1996.

The Legacy hotels also recorded gains in average room rates, up $7.61, or 6%, in 1998 and up $9.47, or 8%, in 1997. These higher rates combined with small increases in occupancy levels to bring RevPAR up 8% to $100.22 in 1998 and 12% to $92.74 in 1997.

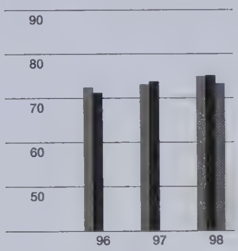
Included in 1998 operating income was $31 million arising from Canadian Pacific Hotels' ownership interest in and management services provided to Legacy. The operating profit from the 11 business hotels now owned by Legacy was $57 million in the period prior to their sale late in 1997 and $43 million in 1996.

At Princess Hotels, the average room rate, occupancy level and RevPAR were $307.23, 52.5% and $161.30, respectively. Delta Hotels operated at 73.3% occupancy with an average room rate of $107.04 for a RevPAR of $78.46. Some of the recently acquired properties have below-average occupancy levels providing opportunity to improve earnings through enhanced management. Together, the newly acquired Princess Hotels and Delta Hotels contributed operating income of $22 million.

In addition to the management and advisory fees generated for services provided to Legacy, other management activities and equity income from hotel partnerships generated revenues of $10 million in 1998 and $6 million in 1997, compared with $2 million in 1996. Results in 1998 included new managed properties – Manoir Richelieu, Glitter Bay and Royal Pavilion. The latter two were acquired as part of the purchase of Princess Hotels. In addition, 1998 results benefited from an expansion at Whistler, British Columbia, but the contract at Deerhurst, Ontario was not renewed.

OCCUPANCY RATES
(%)

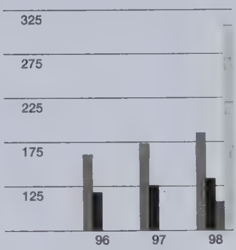
- Canadian Resort Hotels
- Legacy Hotels REIT
- Delta Hotels
- Princess Hotels



	96	97	98
Canadian Resort Hotels	72.4	73.1	74.9
Legacy Hotels REIT	71.2	73.7	75.1
Delta Hotels	–	–	73.3
Princess Hotels	–	–	52.5

AVERAGE ROOM RATES
($)

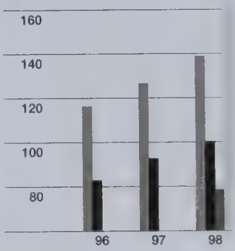
- Canadian Resort Hotels
- Legacy Hotels REIT
- Delta Hotels
- Princess Hotels



	96	97	98
Canadian Resort Hotels	160.65	173.29	185.22
Legacy Hotels REIT	116.37	125.84	133.45
Delta Hotels	–	–	107.04
Princess Hotels	–	–	307.23

REVENUE PER AVAILABLE ROOM
($)

- Canadian Resort Hotels
- Legacy Hotels REIT
- Delta Hotels
- Princess Hotels



	96	97	98
Canadian Resort Hotels	116.31	126.67	138.73
Legacy Hotels REIT	82.83	92.74	100.22
Delta Hotels	–	–	78.46
Princess Hotels	–	–	161.30

Data for 1996 and 1997 are for the current portfolio of properties.

OPERATING EXPENSES

Operating expenses of $371 million in 1998 compared with $429 million in 1997 and $450 million in 1996. The formation of Legacy was a significant factor in the decreases in 1997 and 1998. An offset in 1998 was the acquisition of the Princess and Delta operations. Canadian Pacific Hotels expects to achieve cost saving opportunities in administrative overhead and information systems across the expanded operations.

CAPITAL SPENDING

A number of internal growth projects also took place throughout 1998 and 1997 enhancing the existing core assets. A 221-room new wing at the Chateau Whistler Resort opened in July 1997. The expanded hotel, which now offers 558 rooms and 28,000 square feet of meeting space, was voted the #1 ski resort in North America by *Conde Nast Traveler* magazine in November 1997. Plans are also in place for the addition, pending environmental appeals, of 80 new rooms and a meeting facility at Chateau Lake Louise, and improved guest entrances and enhanced service facilities at Banff Springs. Canadian Pacific Hotels, with its partners, is restoring the Manoir Richelieu and adding a conference centre to the resort and gaming facilities. Canadian Pacific Hotels' share of the total project cost is some $35 million.

The Royal York Hotel opened its nineteenth floor as an executive meeting facility. Built in an area of the hotel that had been vacant for many years, the luxurious facility is an example of how Canadian Pacific Hotels is maximizing the strength of existing assets. Similarly, a swimming pool and health club were constructed at The Palliser, and opened in December 1997.

In 1999, Canadian Pacific Hotels' profit improvement projects will focus on the upgrading of the Princess Hotels' properties and a number of smaller projects at the Canadian mountain resort properties. Legacy also expects to undertake a number of small projects, including guest and meeting room renovations at the Queen Elizabeth Hotel and the redesign of the Imperial Room and adjacent areas at the Royal York.

Canadian Pacific Hotels will also pursue additional management contracts and hotel acquisitions as opportunities arise.

OUTLOOK

Canadian Pacific Hotels continued to report steady profit improvements while undergoing significant changes to become a major player in the international hotel business. It has grown successfully both nationally and internationally and now has over 25,000 rooms under management, providing excellent opportunities for synergies between its brands and for centralizing support services. This strength, together with an industry outlook for increasing international tourism, provides opportunities to enhance Canadian Pacific Hotels' earnings potential.

While there is an uncertain outlook for sustained economic growth, Canadian Pacific Hotels' bookings for 1999 have tracked well against 1998.

Other Consolidated Income Statement Items

OTHER OPERATING INCOME

Consolidated results include operating income from the servicing and sale of land assets of $31 million, or $17 million after tax, in 1998.

NET INTEREST EXPENSE

Net interest expense was $251 million in 1998, $195 million in 1997 and $235 million in 1996 on average net debt of $2,762 million, $2,184 million and $3,336 million, respectively. The increases in 1998 were principally attributable to the investment in business assets financed in part by a higher level of borrowings in addition to the redeployment of proceeds from instalment receipts received from asset sales in 1997. In 1997, corporate debt levels were down because of the sale of Marathon Realty in 1996 and the utilization of some of the proceeds from the sale of Laidlaw and the business hotels.

NON-OPERATING ITEMS

Non-operating expenses were $77 million in 1998, up some $50 million from both 1997 and 1996. Excluding special items, non-operating expenses in 1997 and 1996 were $95 million and $113 million, respectively. 1998 results reflect a reduction in corporate expenses and a reversal of $47 million in information technology costs to offset the subsidiaries' Year 2000 expenses. 1998 results also included an unrealized loss of $61 million on forward foreign exchange contracts that extend to 2002. The loss reflected the sharp decline in the value of the Canadian dollar against the U.S. dollar in 1998. Special items in the three years are detailed on page 27.

INCOME TAXES

Income taxes were $293 million in 1998, $557 million in 1997 and $320 million in 1996. The effective tax rate in 1998 decreased to 26% from 36% in 1997, mainly reflecting favourable tax reassessments. In addition, PanCanadian tax-affected losses that had been incurred by its U.S. businesses for a benefit of some $25 million. As well, there was an increase in offshore earnings that are taxed at a lower rate. In 1997, the effective tax rate increased nine percentage points from 27% in 1996 when the effective tax rate was lower due to the utilization of previously non-tax-affected losses.

MINORITY INTEREST

The interest of shareholders other than the Corporation in the earnings of PanCanadian was $20 million in 1998, $43 million in 1997 and $46 million in 1996. In 1997, the Corporation purchased 597,200 additional PanCanadian shares on the open market in order to maintain its ownership interest at approximately 87%.

Liquidity and Capital Resources

CASH FLOW

In 1998, cash flow was down 8% to $2,025 million from $2,189 million in 1997. Cash from operations increased 56% to $2,716 million. The favourable variations in working capital changes stemmed largely from the collection of instalment receipts pertaining to the sale in 1997 of the business hotels and Laidlaw, that were included in working capital in 1997 and redeployed in 1998. Cash from operations, together with the Corporation's ability to use its strong financial position, supported investing activities totalling $3,369 million, and a share buy-back program that required an outlay of $325 million. During 1997, cash from operations of $1,746 million funded an investing program of $923 million, net of proceeds on asset sales of $2,305 million.

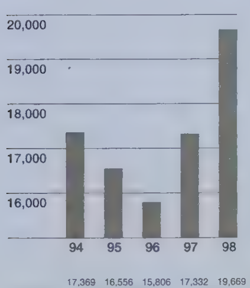
INVESTING ACTIVITIES

Spending on key business acquisitions and investments totalled $1,243 million in 1998 and $698 million in 1997. During 1998, expenditures included $958 million for the purchase by Canadian Pacific Hotels of Princess Hotels and Delta Hotels. Also in 1998, CP Ships acquired Ivaran Lines and ANZDL following its purchase in 1997 of Lykes Lines and Contship Containerlines. During 1997, PanCanadian completed the acquisition of CS Resources. There were other smaller investments in each year.

Additions to properties decreased $128 million to $2,337 million in 1998. Canadian Pacific Railway, which is modernizing its infrastructure and locomotive fleet, increased its outlay by $244 million to $1,102 million. PanCanadian's spending of $894 million was down $351 million, a 28% decline from 1997. As well, the completion late in 1997 of Fording's new wollastonite mine in Mexico contributed to a reduction in its spending, down to $68 million from $223 million. Additions to properties by CP Ships were $125 million in 1998 and $89 million in 1997, and Canadian Pacific Hotels were $117 million in 1998 and $50 million in 1997. Canadian Pacific Hotels' spending in 1998 included $66 million for the two Toronto-area properties.

Proceeds from asset sales amounted to $158 million in 1998, compared to $2,305 million in 1997. Proceeds in 1998 included $65 million at Canadian Pacific Railway, principally from the sale of the British Columbia coastal marine operations, and $60 million at PanCanadian. PanCanadian conducts regular reviews of the economics of production from each of its properties and, in some instances, the value to PanCanadian is enhanced by the sale of the asset. In the prior year, proceeds arose from the sale of the Corporation's investment in Laidlaw for $991 million, sale of the business hotels to Legacy for a net $642 million and non-core asset sales by Canadian Pacific Railway and PanCanadian for $446 million and $209 million, respectively.

CONSOLIDATED ASSETS
($ millions)



FINANCING ACTIVITIES

The consolidated net borrowing position increased to $3,745 million (including cash on hand of $613 million) at December 31, 1998 from $1,779 million at December 31, 1997. The net debt-to-equity ratio moved up to 31:69 at year-end 1998 from 18:82 at year-end 1997. The net debt-to-cash-flow ratio was 1.8:1 at year-end 1998. These ratios demonstrate that Canadian Pacific's cash flow and financial position remained strong in 1998 despite an active acquisition program and a difficult business environment.

The Corporation had $1,088 million of unused short term and long term lines of credit available ($200 million committed) at December 31, 1998 and $163 million of long term debt maturing within one year.

During 1998, 742,164 Common Shares were issued for proceeds of $22 million. PanCanadian raised another $1 million from the issuance of common shares under its stock option plan.

Future Trends, Commitments and Risks

Canadian Pacific expects 1999 to be a year of challenges as the impact of weak economic activity in Asia will continue to adversely affect the commodity-sensitive businesses. However, an ongoing emphasis on capital efficiency and cost control, as well as improved customer service and penetration of new markets, should help mitigate these factors. The largest uncertainty in 1999 relates to oil and natural gas prices at PanCanadian. It is anticipated that the current very low oil price will improve as the year progresses. As well, PanCanadian has protected its cash flow to a significant degree by fixing the prices at attractive levels on a substantial amount of its growing natural gas production. It is expected that capital expenditures will be reduced to some $1.8 billion in 1999, significantly below 1998 levels.

Canadian Pacific's results are affected by external market factors, such as fluctuations in the prices of crude oil, natural gas and coal, as well as by movements in interest and foreign exchange rates. The following table illustrates the estimated effect of changes, under current conditions, in the foreign exchange value of the Canadian dollar, interest rates, and prices of crude oil, natural gas and coal, on consolidated 1999 earnings.

Sensitivity of Consolidated 1999 Net Income *(in millions)*	Effect on Net Income before Hedging	Effect on Net Income after Hedging
U.S.1 cent decrease in the value of the Canadian dollar	$ 22	$ (2)
1 percentage point decrease in interest rates	$ 9	$ 9
U.S.$1.00 per barrel increase in the price of WTI crude oil		
– PanCanadian	$ 31	$ 31
– Other business	$ (8)	$ (8)
10 cent per mcf increase in natural gas prices	$ 16	$ 10
U.S.$1.00 per tonne increase in coal prices	$ 8	$ 8

Canadian Pacific utilizes various derivative financial instruments in order to manage the risks associated with changes in foreign currency exchange rates, interest rates and commodity prices.

Canadian Pacific is exposed to changes in the Cdn./U.S. dollar exchange rate as a result of U.S. dollar revenues, payments associated with long term debt denominated in U.S. dollars and certain other U.S. dollar operating expenditures. This exposure is managed by selling and purchasing forward U.S. dollars at fixed rates in future periods. At December 31, 1998, Canadian Pacific had entered into foreign exchange contracts to sell approximately U.S.$4,312 million at rates ranging from $1.29 to $1.45 over the years 1999 – 2003. Gains and losses relating to these contracts, designated as hedges, are only recognized in income in the period that the hedged exposure is recognized in income. The unrealized loss on these contracts as at December 31, 1998 was $587 million. In addition to the foreign exchange contracts designated as hedges discussed above, Canadian Pacific has entered into foreign exchange contracts, not designated as hedges, to sell U.S.$508 million at rates ranging from $1.29 to $1.31 over the years 1999 – 2002. Gains and losses related to these non-hedged contracts are recognized in income in the current period. As such, $61 million was charged to income for 1998 resulting mainly from the decline in the Cdn./U.S. dollar exchange rate during the year. Additional charges or income relating to these non-hedged contracts will occur in subsequent periods as a result of fluctuations in the exchange rate.

Canadian Pacific is exposed to changes in interest rates as a result of interest payments associated with long term debt. The exposure to interest rate fluctuations is hedged by entering into interest rate and cross currency interest rate swaps which revise the effective interest rates payable. At December 31, 1998, Canadian Pacific had entered into approximately $1,623 million of these swaps relating to long term debt as described in Note 13 on pages 89 to 92 of the 1998 Annual Report. The result of the interest rate swaps has been to convert $1,023 million of long term debt from fixed to floating interest rates. The total unrealized gain with respect to interest rate swaps at December 31, 1998 was $24.5 million.

Canadian Pacific is exposed to changes in commodity prices as a result of fluctuating prices. The exposure to changing oil prices is hedged using New York Mercantile Exchange's (NYMEX) WTI futures contracts and fluctuating differentials for crude oil quality are hedged using over-the-counter (OTC) financial instruments. As at December 31, 1998, Canadian Pacific has sold forward, primarily using NYMEX WTI futures contracts, approximately 0.9 million barrels of crude oil for delivery in 1999 for an average price of U.S.$12.72 per barrel and contracts to purchase approximately 1.8 million barrels of crude oil at prices ranging from U.S.$11.28 to U.S.$18.03 per barrel. Exposure to changing natural gas prices is hedged using primarily OTC financial instruments. As at December 31, 1998, Canadian Pacific has sold forward approximately 366 million cubic feet per day of natural gas over the period January 1999 to March 2000 at an average field gate equivalent price of $2.54 per mcf. In addition, Canadian Pacific has fixed the price on longer term contracts to power generation facilities totalling 30 million cubic feet per day. As at December 31, 1998, the unrealized gain related to commodity instruments was $31 million.

Canadian Pacific is exposed to credit losses in the event of non-performance by counterparties to financial instruments. Canadian Pacific mitigates this risk by dealing with counterparties of high credit quality and requiring credit insurance coverage from the Export Development Corporation or other similar security. In addition, Canadian Pacific deals with an appropriate number of counterparties when entering financial instrument contracts, thereby reducing the risks that would result from concentration.

The long term debt balance at December 31, 1998 comprised foreign currency long term debt (denominated principally in U.S. dollars) of $1,988 million (1997 – $1,786 million) and Canadian dollar debt of $1,475 million (1997 – $1,070 million). Annual maturities and sinking fund requirements for each of the five years following 1998 are: 1999 – $163 million; 2000 – $215 million; 2001 – $443 million; 2002 – $184 million; and 2003 – $511 million.

At December 31, 1998, Canadian Pacific had commitments for capital expenditures amounting to $259 million. Of this amount, $177 million represents the commitment by Canadian Pacific Railway relating to the delivery of 37 new AC locomotives in 1999 for $124 million and an additional $53 million for 16 locomotives in 2001. Also at December 31, 1998, minimum payments under operating leases and gas transportation agreements were estimated at $4,426 million, of which $731 million is payable during 1999 and the remaining $3,695 million becomes payable between 2000 and 2003.

Labour Relations

At the end of 1998, Canadian Pacific Railway had national agreements in place with six out of seven Canadian labour organizations. Five of these are in effect through to the end of 2000 and one to the end of 1999. Negotiations with the Canadian Council of Railway Operating Unions, whose contract expired on December 31, 1998, began in November of 1998 and are ongoing. In the U.S., the company's Soo Line had agreements in effect with 14 of 16 bargaining units. Agreements with unions representing mechanical foremen and signal maintainers expired on December 31, 1998, and significant progress had been made in discussions with both groups. All other agreements extend to the end of 1999. At December 31, 1998, the Delaware & Hudson had agreements with 12 of 14 bargaining units. An agreement with the engineering supervisors was still in negotiation. On December 31, 1998, an agreement with locomotive engineers expired and negotiations are scheduled to begin in February 1999. All of the other agreements do not expire until the end of 1999 or 2000. Most new agreements contain work-rule changes that will significantly increase flexibility and reduce costs.

Fording is party to a number of collective agreements. At the export coal operations, the Fording River and Coal Mountain mines are subject to five-year collective agreements that expire in April 2001 and December 1999, respectively. Negotiations for the Coal Mountain mine are not expected to open until late 1999. The Greenhills mine is not currently unionized. At the prairie operations, a five-year agreement with workers at Whitewood took effect in October 1995 and expires in September 2000, while the Genesee and Mildred Lake operations are currently not unionized. In the U.S., the wollastonite operation in New York is subject to a five-year agreement, which expires in June 2001, and a new five-year agreement with workers at the Tripoli operation took effect July 1998. The new wollastonite facility in Mexico is currently not unionized.

Canadian Pacific Hotels had seven collective agreements expire during 1998. Negotiations for new collective agreements are either underway or soon to be undertaken.

At the Montreal Terminals, workers employed by the Maritime Employer's Association were subject to contracts which expired at the end of December 1997. Negotiations regarding new contracts are still in progress.

Environmental Matters

The Corporation's operations are and will continue to be affected by federal, provincial, state and local laws and regulations regarding the protection of the environment. The Corporation's businesses have policies and procedures in place which support a comprehensive environmental management system that includes audits, legal compliance and reporting. It is not expected that the competitive positions of the Corporation's businesses will be adversely affected within their respective industries by changes to existing laws and regulations where all industry members are subject to the same legislative requirements.

Canadian Pacific Railway is committed to meeting or exceeding government environmental requirements applicable to its operations and activities. In the environmental area, the company complies with legislation and regulations that deal with waste and wastewater management, contaminated sites, spill reporting and emergency response, environmental assessment, storage tanks and other environmental matters. Canadian Pacific Railway has had a comprehensive environmental management program in place since the early 1990s.

As part of this program, based on comprehensive environmental investigations at various sites across Canada and the U.S., Canadian Pacific Railway recorded a $144 million pre-tax charge to earnings in 1995 to cover anticipated expenditures on environmental remediation programs to the year 2005. In 1998, the provision was extended to cover the program until 2008. Sites were classified according to their known environmental condition as well as their past use and level of railway activity. During 1998, approximately $26 million was spent on environmental projects relating to railway operations.

CP Ships has developed a comprehensive program to ensure that procedures for handling hazardous cargo are safe. An emergency response program is in place to deal with any ship- and terminal-related incidents.

PanCanadian is participating in the federal government's Voluntary Challenge Program to reduce greenhouse gas emissions. Emission reductions over the past year were achieved in conjunction with planned capital spending and production optimization projects, thereby minimizing the fiscal impact. In the wake of the Kyoto Protocol and to ensure preparedness, PanCanadian will continue to closely monitor government emission reduction policy developments. A plan for preparedness is in place. Should the Kyoto Protocol be ratified and legislation be proposed, the time frame to meet emission reduction targets is expected to allow an opportunity for PanCanadian to respond. No extraordinary capital expenditures relating to environmental control for existing or new facilities are expected at this time.

At Fording, comprehensive environmental monitoring and mitigation programs ensure that mining activity has a minimal effect on the surrounding natural environment. Through extensive reclamation efforts at each of its operations, mined land is being effectively returned to productive and sustainable uses equal to or better than its pre-mined condition.

Canadian Pacific Hotels has taken or is planning to take corrective action with respect to those hotels that contain friable asbestos; however, the cost of such activities is not expected to be material. Furthermore, Canadian Pacific Hotels has assessed those properties where PCBs may be present in electrical transformers; the cost of corrective action is not expected to be material.

There are not expected to be significant expenditures relating to environmental control on existing or new facilities in the foreseeable future among the Corporation's other businesses.

Litigation

As to be expected during the normal course of business activity, the Corporation and its subsidiaries are occasionally involved in litigation incidental to their respective businesses. Management believes that amounts with respect to such litigation are not material.

Canadian Pacific and the Year 2000 Issue

Canadian Pacific, like most other companies, is vulnerable to the failure of computerized systems or business disruption caused by the Year 2000 issue. The Corporation's Year 2000 program provides for an enterprise-wide focus covering the Canadian Pacific group of companies. Each operating subsidiary has established its own Year 2000 project team to identify and address Year 2000 risks unique to its particular industry and mitigate the potential impact on its operations. Resources dedicated to the effort include internal staff as well as various third-party consultants and professional advisors specialized in dealing with Year 2000 issues. The activities of subsidiary project teams are closely monitored by Canadian Pacific's Year 2000 Task Force, which is chaired by a senior member of management and reports directly to the Board of Directors. The goal of the Task Force is to advance, supervise and coordinate all Year 2000 efforts. PricewaterhouseCoopers has been engaged to assist in the monitoring and validation of Canadian Pacific's Year 2000 program. With this commitment, it continues to be the Corporation's goal to avoid any disruption of services to its customers before, during and after the Year 2000.

THE CORPORATION'S STATE OF READINESS

Canadian Pacific and its subsidiaries developed an approach addressing both Information Systems (IS)-Managed (e.g., computer hardware and software) and Business-Managed (e.g., facilities, embedded systems and third-party business partners) areas separately, but concurrently, with the objective that internal computerized systems, equipment and business processes will be ready for the rollover to the next century. Systems and business processes are considered to be Year 2000 ready when they have been remediated and tested, replaced or retired, or workarounds have been developed.

The Corporation contemplates achieving overall Year 2000 readiness of its critical internal systems by June 30, 1999 so as to provide time for further testing and other initiatives. Remediation and testing of less critical systems, assessment of third-party Year 2000 readiness, and contingency planning efforts for the Year 2000 have been running concurrently and will continue throughout 1999. Management currently believes that Canadian Pacific and its subsidiaries have in place the appropriate plans and resources to achieve timely Year 2000 readiness for its internal computerized systems, equipment and business processes.

The following table shows each subsidiary's readiness or expected readiness dates for its critical internal computerized systems, equipment and business processes:

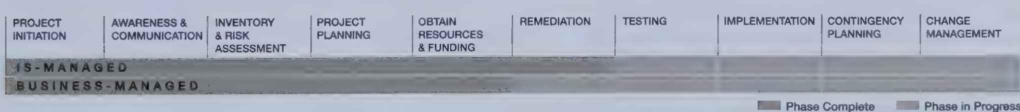
	IS-Managed	Business-Managed
Canadian Pacific Railway	March 31, 1999	March 31, 1999
CP Ships*	June 30, 1999	June 30, 1999
PanCanadian	March 31, 1999	March 31, 1999
Fording	December 31, 1998	December 31, 1998
Canadian Pacific Hotels†	January 31, 1999	January 31, 1999

* *The Year 2000 programs of ANZDL (acquired December 14, 1998) and the joint venture with Transportación Maritima Mexicana (TMM) are currently under review. The overall impact, if any, on CP Ships' Year 2000 readiness is not yet known.*

† *The recently acquired Delta Hotels (acquired May 8, 1998) and Princess Hotels (acquired August 5, 1998) are expected to be Year 2000 ready by June 30, 1999.*

The following charts summarize the Year 2000 progress of Canadian Pacific overall and that of individual operating subsidiaries for both IS-Managed and Business-Managed areas. A description of each phase of Canadian Pacific's Year 2000 program is further described below:

CANADIAN PACIFIC OVERALL YEAR 2000 PROGRESS – DECEMBER 31, 1998



THE TEN PHASES OF CANADIAN PACIFIC'S YEAR 2000 PROGRAM

1. Project Initiation This phase consists of the establishment of a Year 2000 team with the responsibility, management support and authority to successfully complete the project. This includes the development of a framework that incorporates a project management structure, Year 2000 methodology, formal reporting procedures, corporate governance structure, high level plans, general timelines and milestones. This phase is **complete.**

2. Awareness and Communications A starting point in each company has been to raise the awareness of the Year 2000 issue and the type of business relationships, systems and equipment that may be affected by it. This phase also includes communicating Canadian Pacific's Year 2000 readiness to customers, suppliers, investors and other interested parties. The implementation of awareness and communications programs is **complete**. Selected activities are ongoing and will continue into the Year 2000.

3. Inventory and Risk Assessment This phase entails a thorough inventory of computerized systems and business processes including software, hardware and other electronic devices that may be affected by the Year 2000 issue. The inventory is then assessed to determine the criticality of the applicable system or process to the overall operation of the company and to set priorities for those items that need to be addressed first. Where required, the Corporation has engaged third-party consultants with expertise in dealing with specific technology to work with its staff to conduct the inventory. This phase is **complete**, except for recent acquisitions.

4. Project Planning Once the inventory has been gathered and a risk assessment has been completed, a detailed project plan is developed to address the issues identified for both IS-Managed and Business-Managed areas. The project plan outlines the tasks to be completed, the relationship between such tasks and the resources and time required. This phase is **complete**, except for recent acquisitions.

5. Obtain Resources and Funding Project plans are used to estimate resources (both personnel and financial) required to address each particular subsidiary's Year 2000 issues. This phase is **complete** and is described further in "The Costs to Address the Corporation's Year 2000 Issues" section.

6. Remediation At Canadian Pacific, remediation means the repair, replacement or retiring of non-compliant systems, processes or equipment. The remediation effort commences on identification of a Year 2000 issue arising from the prioritized inventory of systems and equipment and is initiated through the project plan. This phase is **complete** for critical systems, except for recent acquisitions and a subsidiary of CP Ships.

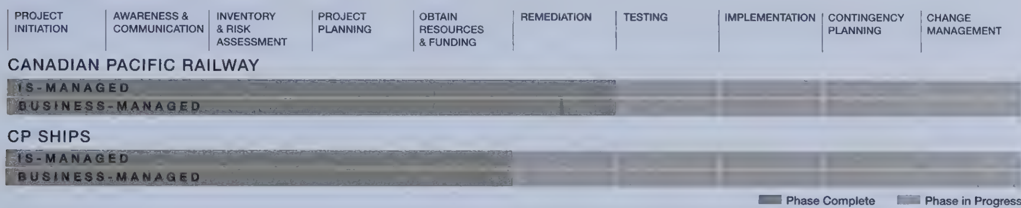
7. Testing This phase includes establishing a test environment and performing tests, which seek to verify that the remediation of a particular system or process was effective. In certain circumstances, the testing of systems and equipment is coordinated with or performed by third-party vendors. Incremental changes to hardware and software components are tested and, as applicable, integration testing of systems interfaces with other systems is conducted. This phase is **in progress**. Additional testing and monitoring activity will continue into the Year 2000.

8. Implementation Implementation is essentially putting the remediated and tested system or asset back into the active business environment. This phase is **in progress**.

9. Contingency Planning Canadian Pacific's contingency planning effort for the Year 2000 entails an assessment of the overall readiness of the Corporation's internal business systems and equipment, and critical business partners, and the Corporation's dependencies thereon. The development of contingency plans is an ongoing process and will continue up to and after the Year 2000. This phase is **in progress** and is further described in "The Corporation's Contingency Plans" section.

10. Change Management This is the process of monitoring that Canadian Pacific's Year 2000 readiness efforts will not be undone by subsequent programming changes or the acquisition of new systems and equipment unless they meet the Corporation's requirements for Year 2000 readiness. This phase is **in progress.** Ongoing change management activities will continue into the Year 2000.

TRANSPORTATION YEAR 2000 PROGRESS – DECEMBER 31, 1998



CANADIAN PACIFIC RAILWAY

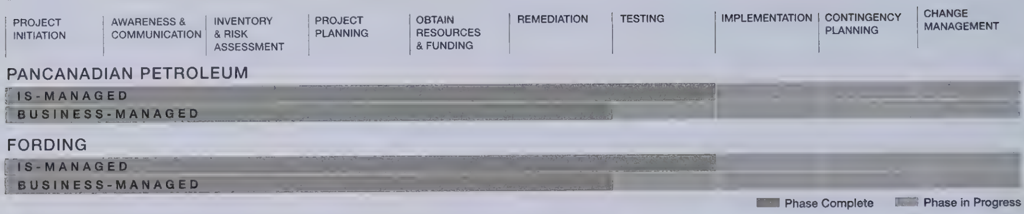
Canadian Pacific Railway continues to progress in accordance with its established Year 2000 plans. As previously reported, major investments in new technology have been made to replace a number of legacy information systems and operating equipment. The remediation and testing of mission critical systems have been substantially completed in 1998 and will continue into 1999 for other less critical systems. Of the essential systems and operating equipment required for the continued safe operation of the railway, impact assessments have indicated that a majority are unaffected by dates or are able to handle dates correctly. Additional testing to verify the readiness of such systems and equipment will continue throughout 1999.

Contingency planning efforts for the Year 2000 have been focused on assessing the readiness of critical third parties such as customers, suppliers, utilities, governmental entities and other third parties. These efforts are ongoing and have been coordinated with the railway's existing business continuity and emergency response plans.

CP SHIPS

CP Ships and its subsidiaries continue to make progress on both its IS-Managed and Business-Managed areas. Cast Lines, however, has reassessed its readiness date to June 30, 1999. Ivaran Lines (acquired May 20, 1998) has been integrated into the Year 2000 program of Lykes Lines. Impact assessments have been completed on its fleet of owned container ships. This assessment, which was completed by a third-party consultant specializing in Year 2000 issues for the maritime industry, has identified certain date-dependent systems that may be affected by the rollover to the next century. These systems will be upgraded or replaced as required or workarounds will be developed. CP Ships continues to assess the readiness of other critical third parties, including the owners of chartered ships, ports, agencies and inland transportation suppliers. Initial assessments have not identified any significant issues; however, such assessments will be an ongoing process that will be closely tied to contingency planning efforts for the Year 2000.

ENERGY YEAR 2000 PROGRESS – DECEMBER 31, 1998



PANCANADIAN PETROLEUM

All areas of PanCanadian's Year 2000 program are progressing well into the remediation, testing, implementation and contingency planning phases. The remediation, testing and implementation of mission critical systems have been substantially completed in 1998 and will continue into 1999 for other less critical systems. The status of remaining hardware and application replacement projects is being closely monitored and current indications are that all projects are proceeding according to schedule. An impact assessment was completed for all major process control systems and site facilities in 1998 with the assistance of an engineering consulting firm specializing in Year 2000 issues for the oil and gas industry. A majority of the remediation work was completed prior to year end and is expected to continue into early 1999.

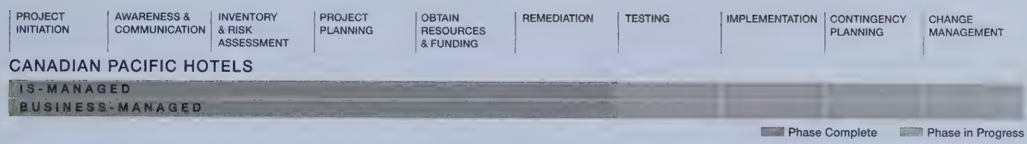
PanCanadian has been developing a comprehensive Year 2000 contingency plan that leverages off existing emergency response and crisis management plans. This plan seeks to minimize the potential adverse impact of the Year 2000 issue on its operations, employees, financial condition and corporate image. The Year 2000 contingency planning effort is closely tied to the readiness assessment of critical third-party service providers such as utilities and pipeline transportation systems.

FORDING

All areas of Fording's Year 2000 program are progressing well into the remediation, testing, implementation and contingency planning phases. The remediation, testing and implementation of mission critical systems have been substantially completed in 1998 and will continue into 1999 for other less critical systems including Business-Managed wollastonite operations whose expected readiness date is June 30, 1999. Initial testing of mine site facilities and operating equipment during annual maintenance shut down did not identify any significant issues. Additional testing to verify the readiness of such systems and equipment will continue throughout 1999.

Fording has completed initial Year 2000 contingency plans for the Year 2000 focused on preventing possible damage due to freezing of its mine site operating facilities and equipment. The Year 2000 contingency planning effort will continue in 1999 and includes the readiness assessment of critical third-party service providers such as utilities, ports and government agencies related to the movement of goods (e.g., customs and port authorities).

HOTELS YEAR 2000 PROGRESS – DECEMBER 31, 1998



CANADIAN PACIFIC HOTELS

Canadian Pacific Hotels continues to make progress on both its IS-Managed and Business-Managed areas. The remediation of mission critical systems at its owned and managed properties have been substantially completed in 1998 and will continue into 1999 for other less critical systems. The status of remaining hardware and application replacement projects is being closely monitored and current indications are that all projects will be completed within the appropriate time frames.

Contingency planning efforts for the Year 2000 are in progress and are being coordinated with existing business continuity plans at individual properties. These efforts are ongoing and will include assessing the readiness of critical third-party relationships such as utilities and suppliers related to the hospitality and travel industry.

THE COSTS TO ADDRESS THE CORPORATION'S YEAR 2000 ISSUES

Canadian Pacific's Year 2000 expenditures include the redeployment of internal resources, incremental costs related to external consultants and professional advisors, and the costs of certain computerized equipment and software for which planned replacement was accelerated due to Year 2000 requirements. The Corporation's Year 2000 readiness effort is being funded entirely by operating cash flows. Remediation costs are expensed, and the cost of new computer hardware, software and equipment is capitalized and amortized over their estimated useful lives.

During the fourth quarter of 1998, all operating subsidiaries were requested to reassess their Year 2000 cost estimates and report to the Task Force. The Corporation estimates that over the life of the project, Year 2000 costs will total $114 million, of which $39 million is expected to be capitalized. The total cost of the Year 2000 program to December 31, 1998 is $47 million, which has been expensed. Canadian Pacific's Year 2000 cost estimate is based on management's current estimates, which are derived from utilizing numerous assumptions of future events and are subject to change.

THE RISKS OF THE CORPORATION'S YEAR 2000 ISSUES

Canadian Pacific, like most other companies, is vulnerable to the failure of its computerized systems and those of key business partners, such as customers, suppliers, utilities, governmental entities and other third parties. Management currently believes that, because of its approach, it will be able to modify or replace its affected internal systems in time to minimize any significant detrimental effects on its operations and that of its subsidiaries. There can, however, be no assurances that the Year 2000 remediation efforts by Canadian Pacific or its key business partners will be successful. Although the impact of the failure to complete such efforts properly or on a timely basis, including the consequences of any litigation that may result, is not yet known, such events could have a material adverse effect on the results of operations, liquidity or financial position of the Corporation.

THE CORPORATION'S CONTINGENCY PLANS

The Corporation is currently reviewing the existing business continuity plans of each operating subsidiary and is supplementing them with plans for Year 2000-related interruptions. This activity is closely tied to the efforts to assess the overall readiness of Canadian Pacific's computerized systems, equipment and business processes and its dependencies on and vulnerabilities to key third-party business partners.

Canadian Pacific's contingency planning for the Year 2000 is addressing various alternatives, including assessing a variety of "most reasonably likely worst case scenarios" to which the Corporation may be required to react, including the failure or disruption of essential third-party services such as electricity and telecommunications. These plans will contemplate the identification of alternative sources of supply for products or services, including increasing inventories and developing additional back-up systems or redundancies. Canadian Pacific's contingency plans for the Year 2000 will evolve throughout the year and will be updated on an ongoing basis.

Canadian Pacific considers the preceding Year 2000 discussion to be a **Year 2000 Readiness Disclosure** within the meaning of the *Year 2000 Information and Readiness Disclosure Act* (United States).

Forward-looking Information

This Annual Report contains certain forward-looking statements within the meaning of the *Private Securities Litigation Reform Act of 1995* (United States) relating, but not limited to, Canadian Pacific's operations, anticipated financial performance, business prospects and strategies. Forward-looking information typically contains statements with words such as "anticipate", "believe", "expect", "plan" or similar words suggesting future outcomes. Much of this information appears under the caption "Management's Discussion and Analysis".

Readers are cautioned not to place undue reliance on forward-looking information because it is possible that predictions, forecasts, projections and other forms of forward-looking information will not be achieved by Canadian Pacific. By its nature, Canadian Pacific's forward-looking information involves numerous assumptions, inherent risks and uncertainties, including, but not limited to, the following factors: changes in business strategies; general global and economic and business conditions; the availability and price of energy commodities; the effects of competition and pricing pressures; industry overcapacity; shifts in market demands; changes in laws and regulations, including environmental and regulatory laws; potential increases in maintenance and operating costs; uncertainties of litigation; labour disputes; timing of completion of capital or maintenance projects; currency and interest rate fluctuations; various events which could disrupt operations, including severe weather conditions; technological changes; and the timely completion of Year 2000 readiness efforts by Canadian Pacific and critical third parties.

Canadian Pacific undertakes no obligation to update publicly or otherwise revise any forward-looking information, whether as a result of new information, future events or otherwise, or the foregoing list of factors affecting such information.

Management's Responsibility for Financial Reporting

The information in this Annual Report is the responsibility of management. The consolidated financial statements have been prepared by management in accordance with Canadian generally accepted accounting principles and include some amounts based on management's best estimates and careful judgement.

Management maintains a system of internal accounting controls to provide reasonable assurance that assets are safeguarded and that transactions are authorized, recorded and reported properly. The internal audit department reviews these accounting controls on an ongoing basis and reports its findings and recommendations to management and the Audit Committee of the Board of Directors.

The Board of Directors carries out its responsibility for the consolidated financial statements principally through its Audit Committee, consisting of five members, all of whom are outside directors. This Committee reviews the consolidated financial statements with management and the independent auditors prior to submission to the Board for approval. It also reviews the recommendations of both the independent and internal auditors for improvements to internal controls as well as the actions of management to implement such recommendations.

Michael A. Grandin
Executive Vice-President and
Chief Financial Officer

David P. O'Brien
Chairman, President and
Chief Executive Officer

February 5, 1999

Statement of Consolidated Income

For the year ended December 31 (in millions, except amounts per share)	1998	1997	1996
Revenues	$ 10,151.0	$ 9,560.0	$ 8,471.3
Cost and expenses			
Cost of goods sold and services	6,432.1	5,829.9	5,021.8
Selling, general and administrative	1,193.2	1,001.7	1,003.1
Depreciation, depletion and amortization	1,084.0	962.7	979.4
	8,709.3	7,794.3	7,004.3
Operating income (Note 2)	1,441.7	1,765.7	1,467.0
Interest expense, net (Note 3)	250.7	194.8	235.3
Non-operating expense (income) (Note 4)	76.8	24.4	25.9
Income before income taxes and minority interest	1,114.2	1,546.5	1,205.8
Income tax expense (Note 5)	292.9	557.0	319.7
Minority interest share of income of subsidiary	20.0	42.8	46.1
Income from continuing operations (Note 2)	801.3	946.7	840.0
Discontinued operations (Note 6)	–	309.1	29.1
Net income	$ 801.3	$ 1,255.8	$ 869.1
Average number of Common Shares outstanding	335.8	345.4	344.4
Earnings per Common Share			
Income from continuing operations	$ 2.39	$ 2.74	$ 2.44
Net income	$ 2.39	$ 3.64	$ 2.52

Statement of Consolidated Retained Income

For the year ended December 31 (in millions, except amounts per share)	1998	1997	1996
Balance, January 1	$ 4,629.1	$ 3,538.6	$ 2,835.3
Net income	801.3	1,255.8	869.1
	5,430.4	4,794.4	3,704.4
Dividends:			
4% Preference Shares	–	–	0.3
Common Shares (per share: 1998 – $0.54; 1997 – $0.48; 1996 – $0.48)	180.8	165.3	165.5
Total dividends	180.8	165.3	165.8
Balance, December 31	$ 5,249.6	$ 4,629.1	$ 3,538.6

See Notes to Consolidated Financial Statements.

Statement of Changes in Consolidated Financial Position

For the year ended December 31 *(in millions)*	1998	1997	1996
Operating Activities			
Income from continuing operations	$ 801.3	$ 946.7	$ 840.0
Depreciation, depletion and amortization	1,084.0	962.7	1,009.4
Deferred income tax expense	158.5	425.3	225.7
Minority interest share of income of subsidiary	20.0	42.8	46.1
Amortization of exchange losses	8.9	20.4	54.8
Gains from sales of businesses, investments and properties	(51.7)	(348.9)	(64.6)
Other	3.8	140.4	(120.4)
Cash flow	2,024.8	2,189.4	1,991.0
Restructuring payments	(116.5)	(173.3)	(231.5)
Other operating activities	(62.1)	37.5	(49.7)
Decrease (increase) in non-cash working capital balances relating to continuing operations (Note 7)	869.5	(307.8)	(134.9)
Cash from continuing operations	2,715.7	1,745.8	1,574.9
Cash from discontinued operations	–	–	35.1
Total cash from operations	2,715.7	1,745.8	1,610.0
Dividends			
Paid to shareholders of the Corporation	(175.0)	(165.9)	(165.2)
Paid to minority shareholders of subsidiaries	(13.9)	(13.5)	(14.7)
	(188.9)	(179.4)	(179.9)
Financing Activities			
Issuance of long term debt	642.6	129.5	216.7
Repayment of long term debt	(225.7)	(934.7)	(832.6)
Issuance of shares by subsidiaries	1.0	9.3	5.4
Buy-back of Common Shares by the Corporation (Note 17)	(324.7)	(272.0)	(2.2)
Issuance of Common Shares by the Corporation (Note 17)	21.7	16.6	48.9
Redemption of Preference Shares by the Corporation	–	–	(14.9)
Other financing activities	–	–	20.6
Discontinued operations (Note 6)	–	–	(104.5)
	114.9	(1,051.3)	(662.6)
Investing Activities			
Business acquisitions and investments (Note 8)	(1,242.7)	(698.2)	(84.7)
Additions to properties (Note 2)	(2,337.1)	(2,465.0)	(1,641.1)
Sales of businesses, investments and properties	157.8	2,304.6	806.9
Other investing activities	53.5	(64.7)	(76.0)
Discontinued operations (Note 6)	–	–	65.4
	(3,368.5)	(923.3)	(929.5)
Cash Position*			
Decrease in cash	(726.8)	(408.2)	(162.0)
Cash at beginning of year	444.4	852.6	1,014.6
Cash at end of year	$ (282.4)	$ 444.4	$ 852.6

* Cash comprises cash and temporary investments net of bank loans and commercial paper.

See Notes to Consolidated Financial Statements.

Consolidated Balance Sheet

December 31 (in millions)	1998	1997
ASSETS		
Current Assets		
Cash and temporary investments	$ 612.8	$ 599.2
Instalment receipts	–	632.0
Accounts receivable	1,545.4	1,583.3
Inventories (Note 9)	478.2	402.2
	2,636.4	3,216.7
Investments (Note 10)	403.9	306.1
Properties, at cost (Note 11)		
Transportation	11,478.8	10,316.6
Energy	11,449.5	10,367.5
Hotels and Real Estate	1,485.1	594.0
Other	213.9	223.0
	24,627.3	21,501.1
Less: Accumulated depreciation, depletion and amortization	9,517.4	8,702.6
	15,109.9	12,798.5
Other Assets and Deferred Charges (Note 12)	1,519.2	1,010.6
	$ 19,669.4	$ 17,331.9

Auditors' Report

To the Shareholders of Canadian Pacific Limited

We have audited the consolidated balance sheets of Canadian Pacific Limited as at December 31, 1998 and 1997 and the statements of consolidated income, consolidated retained income and changes in consolidated financial position for each of the three years in the period ended December 31, 1998. These consolidated financial statements are the responsibility of the Corporation's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management as well as evaluating the overall financial statement presentation.

In our opinion, these consolidated financial statements present fairly, in all material respects, the financial position of Canadian Pacific Limited as at December 31, 1998 and 1997 and the results of its operations and the changes in its financial position for each of the three years in the period ended December 31, 1998 in accordance with generally accepted accounting principles in Canada.

PricewaterhouseCoopers LLP

Chartered Accountants
Calgary, Alberta

February 5, 1999

Consolidated Balance Sheet

December 31 *(in millions)*	1998	1997
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current Liabilities		
Bank loans and commercial paper	$ 895.2	$ 154.8
Accounts payable and accrued liabilities	2,828.1	2,623.8
Income and other taxes payable	136.8	157.5
Dividends payable	51.1	45.3
Long term debt maturing within one year (Note 13)	162.9	169.6
	4,074.1	3,151.0
Deferred Liabilities (Note 14)	1,060.5	979.6
Long Term Debt (Note 13)	3,299.7	2,686.0
Deferred Income Taxes	2,416.3	2,103.3
Deferred Income Credits (Note 15)	463.1	488.0
Minority Shareholders' Interest in Subsidiary Companies (Note 16)	357.7	350.6
Shareholders' Equity (Note 17)		
Common Shares	1,770.2	1,794.4
Paid-in surplus	791.2	1,072.9
Foreign currency translation adjustments	187.0	77.0
Retained income	5,249.6	4,629.1
	7,998.0	7,573.4
Commitments and Contingencies (Notes 20 and 21)		
	$ 19,669.4	$ 17,331.9

See Notes to Consolidated Financial Statements.

Approved on behalf of the Board:

D.P. O'Brien, Director

S.A. Milner, Director

Notes to Consolidated Financial Statements

Note 1. Significant Accounting Policies

Principles of Consolidation

The consolidated financial statements have been prepared in accordance with accounting principles generally accepted in Canada and include the accounts of Canadian Pacific Limited (the Corporation) and all of its subsidiaries (Canadian Pacific). All significant inter-company transactions and balances have been eliminated.

The principal companies included in each business activity are as follows:

December 31 *Percentage Ownership*	**1998**	1997	1996
Transportation			
Canadian Pacific Railway Company	**100.0%**	100.0%	100.0%
CP Ships	**100.0**	100.0	100.0
Energy			
PanCanadian Petroleum Limited	**86.7**	86.7	86.6
Fording Inc.	**100.0**	100.0	100.0
Hotels and Real Estate			
Canadian Pacific Hotels & Resorts Inc.	**100.0**	100.0	100.0

A significant part of Canadian Pacific's exploration, development, production and marketing of oil and gas is carried out as joint ventures and partnerships. These investments are accounted for through proportional consolidation.

The major differences between Canadian and United States generally accepted accounting principles, in so far as they apply to Canadian Pacific, are described under Supplementary Data.

Unless otherwise specified, all dollar amounts are expressed in Canadian dollars.

Revenue Recognition

Transportation: Railway freight revenues are recognized on a percentage of completed service. Revenues from shipping operations, costs directly attributable to loaded container movements and vessel costs, are accounted for on the basis of voyages completed in the period.

Energy: Revenues from crude oil, natural gas and natural gas liquids are recognized at the time of product delivery. Coal sales revenues are recognized when the coal has been loaded and has departed the shipping locations. Industrial minerals sales revenues are recognized upon shipment from the plant.

Hotels: Revenues from hotel operations are recognized when services are provided and ultimate collection is reasonably assured.

Earnings per Common Share

Earnings per Common Share are calculated using the weighted average number of Common Shares outstanding during the year.

Foreign Currency Translation

Foreign currency assets and liabilities of Canadian Pacific's operations, other than through self-sustained foreign subsidiaries, are translated into Canadian dollars at the year-end exchange rate for monetary items and at the historical exchange rates for non-monetary ones. Foreign currency revenues and expenses are translated at the exchange rate in effect on the dates of the related transactions except for provisions for depreciation and depletion which are translated on the same basis as the related assets. With the exception of unrealized gains and losses on long term monetary assets and liabilities, which are being amortized to income over the remaining lives of the related items, foreign currency gains and losses are included in income immediately.

Note 1. Significant Accounting Policies (continued)

The accounts of Canadian Pacific's self-sustained foreign subsidiaries are translated into Canadian dollars using the year-end exchange rate for assets and liabilities and the average exchange rates in effect for the year for revenues and expenses. Exchange gains or losses arising from translation are deferred and included under Shareholders' Equity as Foreign Currency Translation Adjustments. Also included as a foreign currency translation adjustment is the exchange credit arising from translation of Canadian Pacific Railway Company's (Canadian Pacific Railway) Perpetual 4% Consolidated Debenture Stock.

Post Retirement Benefits

For defined benefit plans, pension costs are actuarially determined on the basis of management's best estimates using the projected benefit method prorated over the service lives of employees. Pension expense includes the cost of pension benefits earned during the current year and the amortization of adjustments arising from the pension plan amendments, experience gains and losses and changes in assumptions. The amortization period covers the expected average remaining service lives of employees covered by the various plans. The difference between the market-related value of pension fund assets and the present value of accrued pension benefits, at the date the present accounting policy was adopted, is also being amortized over the expected average remaining service lives of plan employees.

For defined contribution plans, pension costs generally equal plan contributions made during the current year.

For post-retirement health care and life insurance benefits, costs are based on the annual insurance premium paid to provide these benefits.

Inventories

Rail materials and supplies are valued at the lower of average cost and replacement cost.

Finished goods are valued at the lower of average cost and net realizable value.

Properties

Transportation: Fixed asset additions and major renewals are recorded at cost. When railway depreciable property is retired or otherwise disposed of in the normal course of business, the book value, less salvage, is charged to accumulated depreciation.

Depreciation is calculated on the straight-line basis at rates based upon the estimated service lives of depreciable property, except for rail and other track material in the United States which is based on usage.

Equipment under capital lease is included in properties and depreciated over the period of expected use.

Estimated service lives used for principal categories of transportation properties are as follows:

Railway	Years
Diesel locomotives	28 to 32
Freight cars	21 to 43
Ties	35 to 45
Rails in first position	21 to 30
in other than first position	54
Computer system development costs	5 to 10
Ships	20

Note 1. Significant Accounting Policies (continued)

Energy: Canadian Pacific follows the full cost method of accounting for oil and gas properties, whereby all costs relating to the exploration for, and the development of, conventional crude oil and natural gas reserves are capitalized on a country-by-country cost centre basis. Costs accumulated within each cost centre are depleted and depreciated using the unit of production method, based on estimated proved reserves, with net production and reserves volumes of natural gas converted to equivalent energy units of crude oil. Proceeds from disposal of properties are normally deducted from the full cost pool without recognition of gain or loss.

Costs of exploration in new cost centres, together with related land costs, are excluded from costs subject to depletion until it is determined whether or not proved reserves are attributable to the properties, or if impairment has occurred.

In determining the depletion and depreciation provisions for conventional crude oil and natural gas assets, Canadian Pacific includes any excess of the net book value of those oil and natural gas assets over the unescalated, undiscounted future net operating revenues from its proved oil and natural gas reserves for each cost centre (ceiling test). A second ceiling test calculation is conducted on an enterprise basis, by including in the depletion and depreciation provisions any excess of the net book value of conventional oil and natural gas assets for all cost centres over the unescalated, undiscounted future net operating revenues from proved oil and natural gas reserves, less future general and administrative expenses, financing costs and income taxes. The ceiling test calculations utilize Canadian Pacific's weighted average product prices prevailing at year end.

Depreciation of conventional crude oil and natural gas plant, production and other equipment is provided for using the unit of production method. Natural gas liquids extraction facilities are depreciated on a straight-line basis over the estimated service lives of the assets.

Estimated future dismantlement and site restoration costs of conventional crude oil and natural gas assets are provided for using the unit of production method. Such costs for extraction facilities of natural gas liquids are provided for over the estimated service lives of the assets. Expenditures incurred to dismantle facilities and restore well sites are charged against the related restoration liability.

Land, buildings and equipment are recorded at cost. Expenditures to acquire, explore for and develop identified mineral properties are capitalized, net of costs relating to production during the development phase, pending evaluation and completion. Expenditures on general exploration for producing properties and abandoned properties are charged against income.

Depletion on producing mineral properties is provided for using a unit of production method based upon the proved mineral reserve position.

Estimated costs for the reclamation of mineral properties are provided for using the unit of production method.

Interest on funds borrowed to finance major energy projects is capitalized during the development and construction periods.

Hotels: Hotel properties are recorded at cost including interest capitalized during construction of new facilities and major renewals.

The sinking fund method of providing depreciation is used for buildings. This method will amortize the cost of the buildings over a maximum period of 40 years in a series of annual instalments increasing at the rate of 5% compounded annually.

Note 1. Significant Accounting Policies (continued)

Goodwill

Goodwill represents the excess of purchase price over fair value of identifiable assets acquired, and is amortized to income over the estimated periods of benefit. Canadian Pacific evaluates the carrying value of goodwill for possible impairment on an annual basis. Goodwill is written down to fair value when declines in value are considered to be other than temporary based upon expected cash flows of the respective subsidiary.

Financial Instruments

Derivative financial instruments are utilized by Canadian Pacific to manage its exposure to market risks relating to foreign currency exchange rates, interest rates and commodity prices. Unrealized gains and losses on derivative instruments used to convert the Canadian dollar principal of long term debt to United States dollars are amortized into income over the term of the related debt instrument. Unrealized gains and losses on derivative instruments, except those used as hedges, are recognized in income in the current period. Unrealized gains and losses on derivative instruments used as hedges are recognized in income in the period that the hedged exposure is recognized in income, which is the same period as the instrument is settled. The gain or loss is netted against the income or expense item which was hedged. Gains or losses realized on the termination of derivative instruments prior to their maturity are deferred and recognized in the period that the item which was hedged by the terminated instrument is recognized in income.

Restructuring Charges

The present values of future payments towards restructuring charges are recorded in deferred liabilities, and in accrued liabilities when the timing of future payments is known. The discount is being amortized over the payment period.

Note 2. Segmented Information

Canadian Pacific has five reportable segments in three core business activities. The segments are Canadian Pacific Railway, CP Ships, PanCanadian Petroleum Limited, Fording Inc. and Canadian Pacific Hotels & Resorts Inc. Canadian Pacific Railway provides rail and intermodal freight transportation services across Canada and into the U.S. midwest and northeast. CP Ships is a container shipping company operating in the North Atlantic, Latin America and Australasia. PanCanadian Petroleum Limited produces and markets crude oil, natural gas and natural gas liquids in Canada and internationally. Fording Inc. produces metallurgical coal for the international steel industry, thermal coal for electric utilities, and also produces wollastonite and tripoli. Canadian Pacific Hotels & Resorts Inc. operates, in Canada and internationally, full service hotels, some of which are owned.

The accounting policies of the segments are described in the summary of significant accounting policies. Canadian Pacific evaluates performance based on many factors, including net income or loss.

Canadian Pacific's reportable segments are distinct strategic business units that offer different products and services. They are managed separately because of the different operational and marketing strategies required for each segment. The segments are separate legal entities, with any acquisitions being integrated into the segment.

Note 2. Segmented Information (continued)

(in millions)		Revenues	Cost of Goods Sold and Services	Selling, General and Administrative	Depreciation, Depletion and Amortization	Operating Income
Transportation						
Canadian Pacific Railway	**1998**	**$ 3,516.5**	**$ 1,910.0**	**$ 591.5**	**$ 279.0**	**$ 736.0**
	1997	3,716.8	2,049.0	616.5	249.2	802.1
	1996	3,559.4	2,044.6	685.6	226.2	603.0
CP Ships	**1998**	**$ 2,646.7**	**$ 2,018.2**	**$ 396.8**	**$ 70.5**	**$ 161.2**
	1997	1,475.8	1,085.3	195.3	49.6	145.6
	1996	1,113.8	822.6	142.4	37.9	110.9
Total (after elimination of intra-activity charges*)	**1998**	**$ 6,014.4**	**$ 3,779.4**	**$ 988.3**	**$ 349.5**	**$ 897.2**
	1997	5,049.8	2,991.5	811.8	298.8	947.7
	1996	4,536.5	2,730.5	828.0	264.1	713.9
Energy						
PanCanadian Petroleum Limited	**1998**	**$ 2,965.6**	**$ 1,986.1**	**$ 93.4**	**$ 649.7**	**$ 236.4**
	1997	3,238.6	2,076.8	111.0	566.1	484.7
	1996	2,744.2	1,554.3	90.4	624.7	474.8
Fording Inc.	**1998**	**$ 906.1**	**$ 694.6**	**$ 13.8**	**$ 68.5**	**$ 129.2**
	1997	1,017.8	748.5	11.2	61.1	197.0
	1996	915.1	689.1	12.9	50.6	162.5
Total	**1998**	**$ 3,871.7**	**$ 2,680.7**	**$ 107.2**	**$ 718.2**	**$ 365.6**
	1997	4,256.4	2,825.3	122.2	627.2	681.7
	1996	3,659.3	2,243.4	103.3	675.3	637.3
Hotels and Real Estate						
Canadian Pacific Hotels & Resorts Inc.	**1998**	**$ 549.5**	**$ 256.6**	**$ 97.7**	**$ 16.3**	**$ 178.9**
	1997	565.1	324.4	67.7	36.7	136.3
	1996	565.6	338.0	71.8	40.0	115.8
Total of Segments (after elimination of inter-activity charges**)	**1998**	**$10,151.0**	**$ 6,432.1**	**$ 1,193.2**	**$ 1,084.0**	**$ 1,441.7**
	1997	9,560.0	5,829.9	1,001.7	962.7	1,765.7
	1996	8,471.3	5,021.8	1,003.1	979.4	1,467.0
Other	**1998**					
Other activities	1997					
	1996					
Continuing Operations (after inter-company eliminations)	**1998**	**$10,151.0**	**$ 6,432.1**	**$ 1,193.2**	**$ 1,084.0**	**$ 1,441.7**
	1997	9,560.0	5,829.9	1,001.7	962.7	1,765.7
	1996	8,471.3	5,021.8	1,003.1	979.4	1,467.0
Discontinued Operations (Note 6)	**1998**					
	1997					
	1996					
Consolidated Total	**1998**					
	1997					
	1996					

* Charges between entities within the same core activity, or between entities in different core business activities, are made at normal tariff or other arm's length rates. Charges between entities within the same business activity are eliminated in reporting revenues and expenses by business activity. Services provided by entities in the Transportation business activity to other entities in this activity yielded revenues in 1998 of $148.8 million (1997 – $142.8 million; 1996 – $136.7 million).

Interest Expense, Net	Non-Operating Expense (Income)	Income Tax Expense (Recovery)	Minority Interest	Net Income (Loss)	Segment Assets	Additions to Properties
$ 118.5	**$ 18.4**	**$ 231.7**	**$ –**	**$ 367.4**	**$ 8,306.8**	**$ 1,102.3**
119.5	37.3	228.6	–	416.7	7,502.4	858.0
112.8	(43.7)	88.5	–	445.4	7,213.8	555.5
$ (0.7)	**$ 0.4**	**$ 10.2**	**$ –**	**$ 151.3**	**$ 1,803.4**	**$ 125.3**
(3.4)	–	14.3	–	134.7	1,329.4	89.0
(3.1)	–	10.5	–	103.5	645.2	99.1
$ 117.8	**$ 18.8**	**$ 241.9**	**$ –**	**$ 518.7**	**$10,110.2**	**$ 1,227.6**
116.1	37.3	242.9	–	551.4	8,831.8	947.0
109.7	(43.7)	99.0	–	548.9	7,859.0	654.6
$ 99.5	**$ (15.5)**	**$ 15.8**	**$ 20.0**	**$ 116.6**	**$ 6,120.1**	**$ 893.6**
45.9	1.8	120.5	42.8	273.7	5,682.8	1,244.5
47.8	(26.0)	121.3	46.1	285.6	5,037.8	775.6
$ 20.4	**$ 0.1**	**$ 42.8**	**$ –**	**$ 65.9**	**$ 1,170.3**	**$ 68.5**
9.6	(0.4)	70.1	–	117.7	1,118.0	223.4
10.4	(0.4)	58.9	–	93.6	920.6	159.8
$ 119.9	**$ (15.4)**	**$ 58.6**	**$ 20.0**	**$ 182.5**	**$ 7,290.4**	**$ 962.1**
55.5	1.4	190.6	42.8	391.4	6,800.8	1,467.9
58.2	(26.4)	180.2	46.1	379.2	5,958.4	935.4
$ 32.2	**$ 0.3**	**$ 47.8**	**$ –**	**$ 98.6**	**$ 1,944.7**	**$ 117.0**
19.1	(202.6)	156.5	–	163.3	719.7	50.1
24.1	(31.1)	52.8	–	70.0	1,027.5	51.0
$ 269.9	**$ 3.7**	**$ 348.3**	**$ 20.0**	**$ 799.8**	**$19,345.3**	**$ 2,306.7**
190.7	(163.9)	590.0	42.8	1,106.1	16,352.3	2,465.0
192.0	(101.2)	332.0	46.1	998.1	14,844.9	1,641.0
$ (19.2)	**$ 73.1**	**$ (55.4)**	**$ –**	**$ 1.5**	**$ 2,042.1**	**$ 30.4**
4.1	188.3	(33.0)	–	(159.4)	2,346.1	–
43.3	127.1	(12.3)	–	(158.1)	2,639.3	0.1
$ 250.7	**$ 76.8**	**$ 292.9**	**$ 20.0**	**$ 801.3**	**$19,669.4**	**$ 2,337.1**
194.8	24.4	557.0	42.8	946.7	17,331.9	2,465.0
235.3	25.9	319.7	46.1	840.0	15,109.2	1,641.1
				$ –	**$ –**	**$ –**
				309.1	–	–
				29.1	696.7	–
				$ 801.3	**$19,669.4**	**$ 2,337.1**
				1,255.8	17,331.9	2,465.0
				869.1	15,805.9	1,641.1

** Charges between entities in different business activities are not eliminated in reporting revenues and expenses by business activity but are eliminated in reporting total consolidated revenues and expenses. Consolidated net income is not affected by this practice. Services provided by the Transportation business activity to other business activities yielded revenues in 1998 of $284.6 million (1997 – $311.3 million; 1996- $290.1 million).

Note 2. Segmented Information (continued)

Notes

Transportation:

- *Included in revenues of Canadian Pacific Railway, in 1997, is $134.1 million ($99.3 million after tax) of gains from the sale of Kansas City and Corn Lines (KCCL), Molson Centre lease and a portion of the St. Lawrence & Hudson line.*
- *Included in revenues of Canadian Pacific Railway, in 1996, is a $16.7 million gain on the sale of an equity investment in a rail industry insurance association.*
- *Included in non-operating items of Canadian Pacific Railway, in 1996, is a gain of $120.4 million on the repayment of the Perpetual 4% Consolidated Debenture Stock, and a $30 million charge ($16.5 million after tax) to reflect a reduction in the discount rate on previous restructuring accruals.*

Hotels and Real Estate:

- *Included in revenues of Canadian Pacific Hotels & Resorts Inc., in 1998, is $31 million ($17 million after tax) relating to real estate activities.*
- *Included in non-operating items of Canadian Pacific Hotels & Resorts Inc., in 1997, is a $211 million gain ($99.8 million after tax) on disposition of business hotels and, in 1996, is a $31 million gain ($19.6 million after tax) on the sale of shares of Doubletree Corporation.*

Other:

- *Included in non-operating items of other activities, in 1998, is a $60.7 million ($34 million after tax) provision for unrealized foreign exchange losses and $47 million ($26 million after tax) reversal of the 1997 provision for information technology costs to offset charges in the five reportable segments and, in 1997, is an $86 million ($48 million after tax) provision for unrealized foreign exchange losses and $54 million ($30 million after tax) for information technology costs and, in 1996, is $30 million additional amortization of exchange loss on the intended early repayment, in 1997, of U.S.$500 million of debt.*
- *Income tax expense, in 1997, includes a $35 million general tax provision and, for 1996, includes a $25 million general tax provision and a $33 million charge relating to the sale of tax losses to a subsidiary in prior years.*

Geographic Information

(in millions)	**1998**	1997	1996
Canada			
Revenues			
Domestic	**$ 3,611.0**	$ 4,460.3	$ 4,473.1
Export	**1,823.7**	1,833.5	1,615.2
Inter-company revenues	**(400.1)**	(454.1)	(426.8)
	$ 5,034.6	$ 5,839.7	$ 5,661.5
Operating income	**$ 1,187.0**	$ 1,493.9	$ 1,164.9
Total assets	**$ 15,733.8**	$ 14,508.7	$ 13,684.1
United States			
Revenues	**$ 3,444.1**	$ 2,935.0	$ 2,292.6
Operating income	**$ 167.7**	$ 213.7	$ 299.7
Total assets	**$ 3,370.4**	$ 2,858.0	$ 3,066.6
Other Countries			
Revenues	**$ 1,672.3**	$ 785.3	$ 517.2
Operating income	**$ 87.0**	$ 58.1	$ 2.4
Total assets	**$ 2,283.2**	$ 1,331.7	$ 733.5
Summary			
Revenues	**$ 10,151.0**	$ 9,560.0	$ 8,471.3
Operating income	**$ 1,441.7**	$ 1,765.7	$ 1,467.0
Total assets	**$ 21,387.4**	$ 18,698.4	$ 17,484.2
Investment in Laidlaw Inc.	**–**	–	696.7
Inter-company eliminations	**(1,718.0)**	(1,366.5)	(2,375.0)
	$ 19,669.4	$ 17,331.9	$ 15,805.9

Note 3. Interest Expense, Net

(in millions)	1998	1997	1996
Long term debt and debenture stock	$ 270.4	$ 265.2	$ 288.3
Short term debt	29.3	5.5	5.9
	299.7	270.7	294.2
Less: Interest income	49.0	75.9	58.9
	$ 250.7	$ 194.8	$ 235.3

Note 4. Non-operating Expense (Income)

(in millions)	1998	1997	1996
Gain on repayment of the Perpetual 4% Consolidated Debenture Stock	$ –	$ –	$ (120.4)
Gain on sale of Doubletree Corporation shares	–	–	(31.0)
Gain on sale of business hotels	–	(211.0)	–
Information technology costs	(47.0)	54.0	–
Gain on sale of working interest in Syncrude	–	–	(9.0)
Amortization of exchange losses	8.9	20.4	54.8
Other exchange losses (gains)	47.5	76.7	(8.2)
Amortization of the discount of the present value of the restructuring charges	21.1	30.7	61.2
Other	46.3	53.6	78.5
	$ 76.8	$ 24.4	$ 25.9

Note 5. Income Tax Expense

(in millions)	1998	1997	1996
Canadian			
Current	$ 118.2	$ 104.7	$ 80.4
Deferred	153.0	432.0	215.6
	$ 271.2	$ 536.7	$ 296.0
Foreign			
Current	$ 16.2	$ 27.0	$ 13.6
Deferred	5.5	(6.7)	10.1
	$ 21.7	$ 20.3	$ 23.7
Total			
Current	$ 134.4	$ 131.7	$ 94.0
Deferred	158.5	425.3	225.7
	$ 292.9	$ 557.0	$ 319.7
The deferred income tax expense arose from the following:			
Excess of tax over book depreciation	$ 271.2	$ 176.6	$ 97.0
Exploration and development allowances in excess of depletion	(83.5)	99.5	41.7
Losses tax affected	(65.8)	(88.0)	(207.0)
Tax losses utilized	27.0	161.9	109.3
Write-down of assets and restructuring costs	7.0	6.8	–
Reduction in restructuring accruals	44.9	54.7	84.8
Other	(42.3)	13.8	99.9
	$ 158.5	$ 425.3	$ 225.7

Note 5. Income Tax Expense (continued)

The difference between the income tax expense and the provision obtained by applying the statutory tax rate is as follows:

(in millions)	1998	1997	1996
Provision at Canadian statutory rates	**$ 500.0**	$ 691.6	$ 541.4
Depletion and resource allowances	**(80.2)**	(105.2)	(115.0)
Foreign tax rate differentials	**(101.8)**	(76.2)	(51.0)
Royalties and mineral reserve tax	**44.1**	53.7	62.4
Losses (gains) not tax affected	**4.5**	22.8	(44.7)
Previously unrecognized loss carryforwards utilized	**(15.6)**	(116.5)	(141.9)
Large corporation tax	**22.7**	21.0	19.8
Non-deductible amortization of excess of acquisition cost over book value	**5.9**	5.9	5.9
Other, including tax reassessments and provisions	**(86.7)**	59.9	42.8
Income tax expense	**$ 292.9**	$ 557.0	$ 319.7

Note 6. Discontinued Operations

The Corporation completed the sale of its interest in Laidlaw Inc. (Laidlaw) in July 1997. The interest was sold by means of Laidlaw Share Purchase Rights, represented by instalment receipts. The first instalment of $9.45 per share was received on closing and the final instalment of $9.40 per share was received in early July 1998. Net proceeds from the sale amounted to $990.8 million, and resulted in a gain of $271.5 million.

On September 30, 1996, the Corporation completed the sale of the Canadian assets of its wholly-owned real estate subsidiaries, Marathon Realty Company Limited and Centrixx Realty Holdings Limited, collectively "Marathon", at a price of approximately $952 million, including assumed debt. The sale of Marathon's U.S. shopping centre portfolio was also completed for gross proceeds of U.S.$319 million. No gain was booked on the sale of the real estate assets.

The results of discontinued operations are summarized below:

	1997
(in millions)	Laidlaw
Equity in income	$ 37.6
Gain on disposal	271.5
Income tax expense	–
Income from discontinued operations	$ 309.1

Note 6. Discontinued Operations (continued)

	1996		
(in millions)	Laidlaw	Marathon	Total
Revenues	$ –	$ 237.9	$ 237.9
Operating income	–	81.9	81.9
Interest expense, net	–	85.0	85.0
Non-operating income	–	(2.2)	(2.2)
Loss before income taxes, minority interest and equity in income	–	(0.9)	(0.9)
Income tax expense	–	2.8	2.8
Minority interest share of income of subsidiaries	–	1.3	1.3
Loss before equity in income	–	(5.0)	(5.0)
Equity in income	34.1	–	34.1
Net income (loss)	34.1	(5.0)	29.1
Gain (loss) on disposal	–	–	–
Income tax expense	–	–	–
Income (loss) from discontinued operations	$ 34.1	$ (5.0)	$ 29.1

The results of discontinued operations are after deductions for depreciation and amortization of $35 million in 1996.

Financing activities for discontinued operations are:

(in millions)	**1998**	1997	1996
Issuance of long term debt	$ –	$ –	$ 36.3
Repayment of long term debt	–	–	(115.4)
Redemption of shares by subsidiaries	–	–	(25.4)
	$ –	$ –	$ (104.5)

Investing activities for discontinued operations are:

(in millions)	**1998**	1997	1996
Additions to properties	$ –	$ –	$ (43.9)
Sales of businesses, investments and properties	–	–	99.5
Other investing activities	–	–	9.8
	$ –	$ –	$ 65.4

Note 7. Changes in Non-cash Working Capital Balances

(in millions)	1998	1997	1996
(Increase) decrease in current assets:			
Accounts receivable	**$ 37.9**	$ (273.1)	$ (349.8)
Instalment receipts	**632.0**	(632.0)	–
Inventories	**(76.0)**	(23.1)	(18.8)
Increase (decrease) in current liabilities:			
Accounts payable and accrued liabilities	**204.3**	680.5	96.4
Income and other taxes payable	**(20.7)**	(14.6)	23.9
(Increase) decrease in non-cash working capital balances during the year	**777.5**	(262.3)	(248.3)
Decrease (increase) in non-cash working capital balances relating to write-down of assets and restructuring costs	**–**	–	47.3
Increase in non-cash working capital balances relating to reduction in restructuring accruals	**95.8**	83.5	184.1
Non-cash working capital balances of businesses acquired	**(13.3)**	(155.1)	–
Increase in non-cash working capital balances relating to discontinued operations	**–**	–	10.3
Other changes in non-cash working capital balances not relating to continuing operations (mainly from/to current assets/liabilities to/from long term assets/liabilities)	**9.5**	26.1	(128.3)
Increase in non-cash working capital balances relating to continuing operations	**$ 869.5**	$ (307.8)	$ (134.9)

Note 8. Business Acquisitions and Investments

Expenditures on business acquisitions and investments comprise the following:

(in millions)	1998	1997	1996
Shipping companies and other	**$ 284.6**	$ 232.3	$ 84.7
Princess Hotels	**865.2**	–	–
Delta Hotels	**92.9**	–	–
CS Resources Limited	**–**	465.9	–
	$ 1,242.7	$ 698.2	$ 84.7

Effective November 1, 1998, Canadian Pacific acquired the trade and certain net assets of Australia-New Zealand Direct Line and on May 20, 1998 acquired the trade and certain net assets of Ivaran Lines. The total acquisition cost of these two container shipping businesses and other minor acquisitions amounted to $284.6 million. The excess of total cost over fair value, which includes restructuring and other costs, amounted to $227 million. It has been allocated to goodwill and is being amortized over 35 years. The results of the shipping acquisitions have been included in the Transportation business activity, under CP Ships, from the dates of acquisition.

On August 5, 1998, Canadian Pacific acquired for $865.2 million seven Princess resort properties of which five are 100% owned and two are 49% owned. The excess of total cost over fair value amounting to $77.4 million has been allocated to goodwill and is being amortized over 40 years. The results of Princess have been included in the Hotels and Real Estate business activity, under Canadian Pacific Hotels & Resorts Inc., from the date of acquisition.

Note 8. Business Acquisitions and Investments (continued)

On May 7, 1998, Canadian Pacific acquired Delta Hotels which manages, franchises and licences 31 properties. The total acquisition cost was $92.9 million and included the management company, the "Delta Hotels" brand and three leasehold hotels. The excess of total cost over fair value amounting to $43.6 million has been allocated to goodwill and is being amortized over 40 years. The results of Delta have been included in the Hotels and Real Estate business activity, under Canadian Pacific Hotels and Resorts Inc., from the date of acquisition.

The 1998 acquisitions have been accounted for as follows:

(in millions)	Princess	Delta	Shipping and Other	Total
Assets Acquired:				
Net current assets	$ 6.0	$ –	$ –	$ 6.0
Investments	16.8	–	71.9	88.7
Net properties	765.0	22.2	42.0	829.2
Goodwill	77.4	43.6	227.0	348.0
Other long term assets	–	34.0	–	34.0
Liabilities Acquired:				
Net current liabilities	–	(6.9)	(29.3)	(36.2)
Long term debt	–	–	(27.0)	(27.0)
Total acquisition cost	$ 865.2	$ 92.9	$ 284.6	$ 1,242.7

On October 29, 1997, Canadian Pacific acquired 100% of the issued and outstanding shares of Contship Containerlines Limited and on July 29, 1997, acquired the assets of Lykes Lines, as part of Lykes' Chapter 11 bankruptcy reorganization. The total acquisition cost of these two container shipping businesses and other minor acquisitions amounted to $232.3 million. The excess of total cost over fair value, which includes restructuring and other costs, amounted to $333.2 million. It has been allocated to goodwill and is being amortized over 35 years. The results of the shipping acquisitions have been included in the Transportation business activity, under CP Ships, from the dates of acquisition.

Effective July 15, 1997, Canadian Pacific acquired 100% of the issued and outstanding shares of CS Resources Limited for $465.9 million. The results of CS Resources Limited have been included in the Energy business activity, under PanCanadian Petroleum Limited, from the date of acquisition.

The 1997 acquisitions have been accounted for as follows:

(in millions)	CS Resources	Shipping and Other	Total
Assets Acquired:			
Net current assets	$ 14.0	$ –	$ 14.0
Investments	–	47.1	47.1
Net property, plant and equipment	537.6	76.6	614.2
Goodwill	–	333.2	333.2
	551.6	456.9	1,008.5
Liabilities Acquired:			
Net current liabilities	–	(162.1)	(162.1)
Long term debt	(57.0)	(62.5)	(119.5)
Other long term liabilities	(28.7)	–	(28.7)
Total acquisition cost	$ 465.9	$ 232.3	$ 698.2

Note 9. Inventories

(in millions)	1998	1997
Rail materials and supplies	$ 194.6	$ 173.0
Raw materials and work in progress	41.0	38.1
Finished goods	170.2	132.3
Stores and materials	72.4	58.8
	$ 478.2	$ 402.2

Note 10. Investments

(in millions)	1998	1997
Accounted for on the equity basis:		
Legacy Hotels Real Estate Investment Trust	$ 109.9	$ 99.9
I&M Rail Link, LLC	36.1	19.6
CNCP Niagara-Detroit Partnership	35.9	40.1
Indiana Harbor Belt Railroad Company	29.4	23.5
Other	68.0	31.4
Accounted for on the cost basis	124.6	91.6
	$ 403.9	$ 306.1

Note 11. Properties and Accumulated Depreciation, Depletion and Amortization

	1998			1997
(in millions)	Cost	Accumulated Depreciation, Depletion and Amortization	Net	Net
Transportation				
Canadian Pacific Railway	$ 10,803.1	$ 3,810.6	$ 6,992.5	$ 6,121.7
CP Ships	675.7	216.7	459.0	324.1
	11,478.8	4,027.3	7,451.5	6,445.8
Energy				
PanCanadian Petroleum Limited	10,077.1	4,790.7	5,286.4	4,873.2
Fording Inc.	1,372.4	493.0	879.4	855.3
	11,449.5	5,283.7	6,165.8	5,728.5
Hotels and Real Estate				
Canadian Pacific Hotels & Resorts Inc.	1,485.1	187.4	1,297.7	429.2
Other	213.9	19.0	194.9	195.0
	$ 24,627.3	$ 9,517.4	$ 15,109.9	$ 12,798.5

Note 12. **Other Assets and Deferred Charges**

(in millions)	1998	1997
Unamortized exchange loss	**$ 293.9**	$ 160.7
Goodwill, net of amortization	**804.6**	456.2
Prepaid pension cost	**122.5**	151.6
Long term receivables and deposits	**65.7**	101.5
Unamortized discount on long term debt and issue costs	**16.9**	11.3
Deferred charges	**55.5**	67.0
Systems development	**60.1**	43.0
Other	**100.0**	19.3
	$ 1,519.2	$ 1,010.6

Note 13. **Long Term Debt**

(in millions)	1998	1997
Canadian Pacific Railway Company		
6.875% – 9.45% Debentures due 2003 – 2022	**$ 1,162.5**	$ 1,072.5
Perpetual 4% Consolidated Debenture Stock	**64.6**	59.6
Obligations under capital leases due 1999 – 2014	**280.0**	266.4
CP Ships		
Obligations under capital leases due 1999 – 2008	**79.0**	61.0
PanCanadian Petroleum Limited		
5.5% – 8.4% medium term notes due 2001 – 2008	**831.0**	486.0
8.75% – 10.55% Debentures due 2000 – 2005	**350.0**	350.0
Commercial paper	**162.8**	50.5
Bank loans	**37.2**	36.8
Other long term financing	**–**	44.3
Canadian Pacific Hotels & Resorts Inc.		
8.84% – 9.5% bank loans due 1999 – 2016	**154.1**	–
Canadian Pacific Limited		
10.5% Debentures due 2001	**250.0**	250.0
Canadian Pacific Enterprises Limited		
8.67% Debentures due 1998	**–**	27.5
Canadian Pacific Securities Limited		
10.75% – 11.6% Guaranteed Debentures due 1999 – 2026	**88.5**	147.8
Other	**2.9**	3.2
	3,462.6	2,855.6
Less: Long term debt maturing within one year	**162.9**	169.6
	$ 3,299.7	$ 2,686.0

The Corporation's and Canadian Pacific Railway's debentures are unsecured, but carry a negative pledge. U.S.$250 million of Canadian Pacific Railway's debentures are callable starting in 2002 at a premium which declines over time. .

Canadian Pacific Railway, through a number of interest rate swaps, converted U.S.$295 million of its long term debt with fixed interest rates from 7.51% to 7.68% into floating interest rates based on U.S. LIBOR and $40.8 million of its long term debt with fixed interest rates from 7.93% to 8.10% into floating based on Bankers' Acceptance rates.

Note 13. Long Term Debt (continued)

Canadian Pacific Railway's Perpetual 4% Consolidated Debenture Stock constitutes a first charge upon and over the whole of the undertaking, railways, works, rolling stock, plant, property and effects of Canadian Pacific Railway, with certain exceptions.

Canadian Pacific Railway's obligations under capital leases bear fixed interest rates which vary from 6.85% to 12.7% and CP Ships' obligations under capital leases bear fixed interest rates which vary from 5% to 15%.

A series of forward foreign currency exchange, interest rate swap and cross currency interest rate swap transactions have been entered into with respect to PanCanadian Petroleum Limited's (PanCanadian) 10.55% Debentures due 2000 amounting to $150 million, which result in an effective interest rate of 8.33% on U.S.$109.5 million.

With respect to U.S.$100 million of PanCanadian's medium term notes with a fixed interest rate of 7.645%, an interest rate swap transaction was entered into and subsequently cancelled and an option was sold but never exercised, resulting in an effective interest rate of 6.48%. PanCanadian, through a series of interest rate and cross-currency interest rate swaps, converted another $100 million of medium term notes with a fixed interest rate of 8.4% into U.S.$73.1 million with an effective interest rate of 5.33%, and converted a further $100 million of medium term notes with a fixed interest rate of 7.5% into U.S.$73 million with an effective rate of U.S. three-month LIBOR minus 93 basis points. In addition, PanCanadian converted $100 million and $225 million with fixed interest rates of 5.5% and 5.8%, respectively, and entered into a series of interest rate and cross-currency interest rate swap transactions. The swap transactions converted the $100 million medium term note into U.S.$71 million with an effective interest rate of U.S. three-month LIBOR minus 49 basis points and the $225 million medium term note into U.S.$71 million and $125 million which resulted in effective interest rates of U.S. three-month LIBOR minus 52 basis points and 5.8%, respectively.

PanCanadian's debentures and medium term notes are unsecured, but carry a negative pledge.

At December 31, 1998, foreign currency long term debt, denominated principally in U.S. dollars, amounted to $1,987.8 million (1997 – $1,786.1 million).

Annual maturities and sinking fund requirements for each of the five years following 1998 are: 1999 – $162.9 million; 2000 – $215.2 million; 2001 – $442.5 million; 2002 – $183.9 million; 2003 – $510.7 million.

In addition to the financial instruments associated with the long term debt referred to above, the Corporation and a number of its subsidiaries are parties with major financial institutions to other financial instruments with off-balance sheet risk as discussed below.

Commodity Instruments

Exposure to changing crude oil prices is hedged using New York Mercantile Exchange's (NYMEX) West Texas Intermediate (WTI) futures contracts. As at December 31, 1998, Canadian Pacific has sold forward, primarily using NYMEX WTI futures contracts, approximately 0.9 million barrels of crude oil for delivery in 1999 for an average price of U.S.$12.72 per barrel, and contracts to purchase approximately 1.8 million barrels of crude oil at prices ranging from U.S.$11.28 to U.S.$18.03 per barrel. Exposure to changing natural gas prices is hedged using primarily over the counter financial instruments. As of December 31, 1998, Canadian Pacific has sold forward approximately 366 million cubic feet per day of natural gas over the period of January 1999 to March 2000 at an average field gate equivalent price of $2.54 per mcf. As at December 31, 1998, the unrealized gain related to commodity instruments was $30.6 million.

Note 13. Long Term Debt (continued)

Forward Foreign Currency Exchange Contracts

Exposure to changes in the Cdn./U.S. dollar exchange rate on future commodity revenue streams and long term debt denominated in U.S. dollars is managed by selling or purchasing forward U.S. dollars at fixed rates in future periods. As at December 31, 1998, Canadian Pacific had entered into foreign exchange contracts to sell approximately U.S.$4,820.2 million at rates ranging from 1.29 to 1.45 over the years 1999 – 2003. As at December 31, 1998, the unrealized loss on forward foreign currency exchange contracts not recognized in income was $587.3 million.

Credit Risk Management

Canadian Pacific is exposed to credit losses in the event of non-performance by counterparties to financial instruments including interest rate swaps on certain inter-company debt; however, Canadian Pacific does not anticipate such non-performance because of dealing with counterparties of high credit quality. In addition, Canadian Pacific does not believe that there are any significant concentrations of credit risk.

Interest Rate Exposure and Fair Values

Canadian Pacific's exposure to interest rate risk along with the total carrying amounts and fair values of its financial instruments are summarized in the following table:

		Fixed Interest Rate Maturing In:					
(in millions)	Floating Interest Rate	Less Than One Year	One to Five Years	More Than Five Years	Non-Interest Bearing	Total Carrying Value	Fair Value
Financial Assets							
Cash and short term investments	$ 612.8	$ –	$ –	$ –	$ –	$ 612.8	$ 612.8
Accounts receivable	–	42.4	–	–	1,503.0	1,545.4	1,545.4
Other assets	–	–	–	–	65.7	65.7	65.7
Financial Liabilities							
Bank loans	(895.2)	–	–	–	–	(895.2)	(895.2)
Accounts and other payables	–	–	–	–	(3,015.9)	(3,015.9)	(3,015.9)
Long term debt	(200.0)	(162.9)	(1,452.6)	(1,647.1) (1)	–	(3,462.6)	(3,747.2)
Derivative Instruments							
Interest rate swaps on long term debt	(1,023.1)	–	100.0	923.1 (2)	–	–	24.5
Forward foreign currency contracts	–	–	–	–	–	–	(587.3)
Commodity instruments	–	–	–	–	–	–	30.6

(1) Includes $64.6 million of Perpetual 4% Consolidated Debenture Stock with no maturity date.

(2) Interest rate swaps totalling $498.1 million, for debt maturing in more than five years, expire as follows: 1999 – $302.3 million; 2000 – $155 million; 2003 – $40.8 million.

For 1997, the fair value of short term financial assets and liabilities was estimated to equal the carrying value on the balance sheet. The fair values for 1997 of long term debt, interest rate swaps, forward foreign currency contracts and commodity instruments were $3,133 million, $69.5 million, $(189) million and $39.5 million, respectively.

Canadian Pacific has determined the estimated fair value of its financial instruments based on appropriate valuation methodologies. However, considerable judgment is necessary to develop these estimates. Accordingly, the estimates presented herein are not necessarily indicative of what Canadian Pacific could realize in a current market exchange. The use of different assumptions or methodologies may have a material effect on the estimated fair value amounts.

Note 13. Long Term Debt (continued)

The following methods and assumptions were used to estimate the fair value of each class of financial instrument:

- Short term financial assets and liabilities are valued at their carrying amounts as presented in the Balance Sheet, which are reasonable estimates of fair value due to the relatively short period to maturity of these instruments.
- The fair value of publicly traded long term debt is determined based upon market prices at December 31, 1998. The fair value of other long term debt is estimated based on rates currently available to Canadian Pacific for long term borrowing with similar terms and conditions to those borrowings in place at the balance sheet date.
- The fair value of derivative instruments is estimated as the discounted unrecognized gain or loss calculated based on market prices or rates at December 31, 1998, which generally reflects the estimated amounts that Canadian Pacific would receive or pay to terminate the contracts at the balance sheet date.
- Although commodity futures are not financial instruments, they have been included as they would represent a material financial liability if terminated.

Note 14. Deferred Liabilities

(in millions)	**1998**	1997
Provision for restructuring costs	**$ 260.6**	$ 284.8
Future removal and site restoration costs	**302.4**	276.2
Deferred workers' compensation	**62.7**	64.9
Deferred hedging gains	**25.5**	36.0
Information technology costs	**7.0**	54.0
Deferred revenue	**7.5**	36.7
Unrealized loss on forward exchange contracts	**147.1**	86.4
Other	**247.7**	140.6
	$ 1,060.5	$ 979.6

Note 15. Deferred Income Credits

Deferred Income Credits include $151.9 million (1997 – $155.3 million) from the Federal Government primarily for the rehabilitation of certain western branch lines, $182.5 million (1997 – $217.4 million) from other bodies, mainly for relocation of railway lines, $59.7 million (1997 – $61.2 million) in investment tax credits and $46.1 million (1997 – $51.7 million) in surplus accumulated depreciation. These amounts are being amortized to income on the same basis as the related properties are being depreciated.

Note 16. Minority Shareholders' Interest in Subsidiary Companies

(in millions)	**1998**	1997
PanCanadian Petroleum Limited	**$ 356.3**	$ 349.2
Other	**1.4**	1.4
	$ 357.7	$ 350.6

Note 17. Shareholders' Equity

The Corporation's articles were amended on July 4, 1996, to change the classes and number of shares authorized for issuance to an unlimited number of Common Shares and an unlimited number of First Preferred Shares and Second Preferred Shares.

Note 17. Shareholders' Equity (continued)

Also on July 4, 1996, the Corporation completed an arrangement under Section 192 of the Canada Business Corporations Act with Canadian Pacific Railway Company (Old CPL) in connection with a reorganization (the Reorganization) which resulted in the Corporation becoming the parent corporation of Old CPL, CP Ships Inc., PanCanadian Petroleum Limited, Fording Coal Holdings Inc., and Canadian Pacific Hotels & Resorts Inc. As part of the Reorganization, the Ordinary Shares of Old CPL were exchanged for Common Shares of the Corporation on a one for one basis and the Preference Shares of Old CPL were converted into Common Shares of the Corporation at a ratio of 4.263 Preference Shares for each Common Share. Holders of Old CPL's Consolidated Debenture Stock elected to either (i) exchange their Consolidated Debenture Stock for cash or Common Shares of the Corporation or (ii) retain their Consolidated Debenture Stock with no change to the terms thereof and with the support of bank letters of credit. Following the Reorganization, the Corporation held, directly or indirectly, on a consolidated basis, the same assets and was subject to the same liabilities as Old CPL prior to the Reorganization.

At December 31, 1998, 1997 and 1996, no First Preferred Shares or Second Preferred Shares were outstanding.

An analysis of Common Share balances is as follows:

	1998		1997		1996	
(in millions)	**Number**	**Amount**	Number	Amount	Number	Amount
Balance, January 1	**340.7**	**$ 1,794.4**	346.9	$ 1,814.4	342.3	$ 1,767.7
New issue	**0.3**	**8.0**	–	–	3.3	19.5
Issued under dividend reinvestment and share purchase, and stock option plans	**0.5**	**13.7**	0.8	16.6	1.4	29.4
Share repurchase plans	**(8.8)**	**(45.9)**	(7.0)	(36.6)	(0.1)	(2.2)
Balance, December 31	**332.7**	**$ 1,770.2**	340.7	$ 1,794.4	346.9	$ 1,814.4

The Corporation has a Dividend Reinvestment and Share Purchase Plan which permits participants to acquire new Common Shares of the Corporation by reinvesting cash dividends paid on Common Shares held by them and by investing optional cash payments, to a maximum of $30,000 in any calendar year.

On July 24, 1996, the Corporation entered into a Normal Course Issuer Bid to repurchase up to 10 million of its Common Shares, representing about 3% of its Common Shares then outstanding. In 1997, 1.8 million shares were repurchased under this plan at a cost of $60.5 million, of which $8.1 million was charged to Common Shares and $52.4 million to Paid-in Surplus.

On August 12, 1997, the Corporation entered into a Normal Course Issuer Bid to repurchase up to 18 million of its Common Shares, representing about 5.3% of its Common Shares then outstanding. In 1998, 6.2 million (1997 – 5.2 million) shares were repurchased under this plan at a cost of $240.7 million (1997 – $211.5 million), of which $34 million was charged to Common Shares and $206.7 million to Paid-in Surplus (1997 – $28.5 million to Common Shares and $183 million to Paid-in Surplus).

On August 11, 1998, the Corporation announced a Normal Course Issuer Bid to repurchase up to 16.6 million of its Common Shares, representing about 5% of its Common Shares then outstanding. Purchases may be made at market prices on the Toronto, Montreal, Vancouver, Alberta, and the New York stock exchanges over the 12 months following regulatory approvals which were granted in mid-August. As of December 31, 1998, 2.6 million shares had been repurchased under this plan at a cost of $84 million of which $11.9 million was charged to Common Shares and $72.1 million to Paid-in Surplus.

Note 17. **Shareholders' Equity** (continued)

Foreign Currency Translation Adjustments: An analysis of the Foreign Currency Translation Adjustments balance is as follows:

(in millions)	1998	1997	1996
Balance, January 1	**$ 77.0**	$ 67.6	$ 204.5
Effect of exchange rate changes	**110.0**	26.2	(13.3)
Release of exchange into income on the repayment of the Perpetual 4% Consolidated Debenture Stock	**–**	–	(101.0)
Discontinued operation	**–**	(16.8)	(22.6)
Balance, December 31	**$ 187.0**	$ 77.0	$ 67.6

Note 18. Stock Options

Under the Corporation's stock option plan, options may be granted to certain key employees to purchase Common Shares of the Corporation at a price not less than the market value of the shares at the grant date. Each option may be exercised after two years in respect of one-half of the number of shares to which it relates and after three years in respect of the balance. Options expire ten years after the grant date.

Simultaneously, with the grant of an option, employees are also granted Share Appreciation Rights (SARs) equivalent to one-half the number of shares to which each option relates. A SAR entitles the holder to receive payment of an amount equal to the excess of the market value of a Common Share at the time of exercise of the SAR over the related option price. SARs may be exercised no earlier than three years and no later than ten years after the grant date.

Where an option has been exercised as to one-half the number of shares to which it relates, any further exercise reduces the number of SARs granted on a one-for-one basis. At all times, the exercise of a SAR reduces the number of shares covered by an option on a one-for-one basis.

In the event of a change in control of the Corporation, all outstanding options and SARs become immediately exercisable.

At December 31, 1998, 3,694,597 shares (1997 – 4,007,451) were available for the granting of future options under the stock option plan out of the 12,000,000 Common Shares originally authorized.

At December 31, 1998, options covering 5,027,528 (1997 – 5,004,702) Common Shares were outstanding. These options expire in the years 1999 to 2008 and are exercisable at prices ranging from $16.125 to $40.850 per share.

Details of the stock options outstanding were as follows:

	1998	1997
Outstanding at beginning of year	**5,004,702**	4,479,064
Granted	**554,300**	2,162,298
Exercised	**(290,028)**	(587,494)
Cancelled	**(241,446)**	(1,049,166)
Outstanding at end of year	**5,027,528**	5,004,702

Options covering 2,311,330 (1997 – 2,434,837) Common Shares were exercisable at December 31, 1998, at a weighted average option price of $21.524 (1997 – $21.149) per share.

Note 19. Pensions

The Corporation and the majority of its subsidiaries have defined benefit plans which provide for pensions based principally on years of service and compensation rates near retirement. Annual contributions to these plans, which are based on various actuarial cost methods, are made on the basis of not less than the minimum amounts required by Federal or Provincial pension supervisory authorities.

Net pension expense from continuing operations for the year for such defined benefit plans includes the following components:

(in millions)	1998	1997	1996
Service cost – benefits earned during the year	$ 27.7	$ 26.6	$ 27.5
Interest cost on projected benefit obligation	416.7	252.8	334.1
Actual return on pension fund assets	(440.8)	(566.1)	(747.2)
Net amortization and deferrals	9.2	352.7	467.4
Net pension expense	$ 12.8	$ 66.0	$ 81.8

The following table sets forth the plans' funded status and the amounts recognized in Canadian Pacific's Consolidated Balance Sheet as at December 31:

	1998		1997	
(in millions)	Plans having assets in excess of accumulated benefits	Plans having accumulated benefits in excess of assets	Plans having assets in excess of accumulated benefits	Plans having accumulated benefits in excess of assets
Average present value of benefit obligations:				
Vested	$ 4,326.4	$ 218.1	$ 4,344.8	$ 35.1
Non-vested	4.9	4.6	7.8	–
Accumulated benefit obligation	4,331.3	222.7	4,352.6	35.1
Effect of projected future salary increases	420.1	35.8	398.2	8.4
Projected benefit obligation (based on weighted average discount rate of approximately 8% and a weighted average salary increase of approximately 2%)	4,751.4	258.5	4,750.8	43.5
Pension fund assets at market related values	5,140.2	162.0	4,889.7	31.3
Pension fund assets greater than (less than) projected benefit obligation	388.8	(96.5)	138.9	(12.2)
Unamortized portion of net obligation at January 1, 1987*	37.4	15.6	106.5	3.5
Unamortized prior service cost*	150.5	1.0	119.4	9.6
Unamortized net (gain) loss*	(352.2)	(22.1)	(215.4)	1.3
Prepaid pension cost in Consolidated Balance Sheet	$,224.5	$ (102.0)	$ 149.4	$ 2.2

* Being amortized over expected average remaining service lives of employees, generally 13 years.

Pension fund assets consist primarily of listed stocks and bonds. The assumed weighted average long term rate of return on pension fund assets is approximately 8%.

Note 19. Pensions (continued)

Canadian Pacific also has subsidiary-sponsored defined contribution plans. Pension expense from continuing operations for such plans, which generally equals the employer's required contribution, was $9.7 million, $8.5 million and $8 million in 1998, 1997, and 1996, respectively.

In addition to pension benefits, the Corporation and several of its subsidiaries provide health care and life insurance benefits for certain retired employees. The cost of providing these benefits is recognized by expensing the annual insurance premiums which were approximately $10.6 million, $10 million and $13 million in 1998, 1997, and 1996, respectively.

Note 20. Commitments and Contingencies

At December 31, 1998, commitments for capital expenditures amounted to $258.9 million and minimum payments under operating leases and gas pipeline transportation agreements were estimated at $4,425.7 million in the aggregate, with annual payments in each of the five years following 1998 of: 1999 – $731 million; 2000 – $556 million; 2001 – $480.5 million; 2002 – $390.2 million; 2003 – $331.5 million.

At December 31, 1998, unused lines of credit for short term and long term financing, subject to periodic review, repayable on demand and at various maturities, amounted to $1,088 million on which interest rates vary with bank prime or money market rates.

Note 21. Uncertainty Due to the Year 2000 Issue

The Year 2000 issue arises because many computerized systems use two digits rather than four to identify a year. Date sensitive systems may recognize the year 2000 as 1900 or some other date, resulting in errors when information using year 2000 dates is processed. In addition, similar problems may arise in some systems which use certain dates in 1999 to represent something other than a date. The effects of the Year 2000 issue may be experienced before, on or after January 1, 2000, and, if not addressed, the impact on operations and financial reporting may range from minor errors to significant systems failure, which could affect Canadian Pacific's ability to conduct normal business operations. It is not possible to be certain that all aspects of the Year 2000 issue affecting Canadian Pacific, including those related to the efforts of customers, suppliers or other third parties, will be fully resolved.

Note 22. Reclassification

Certain prior years' figures have been reclassified to conform with the presentation adopted for 1998.

Note 23. Supplementary Data

The discussion of Canadian and United States accounting principles and the reconciliation of net income between United States and Canadian generally accepted accounting principles for the years included in Supplementary Data are an integral part of these financial statements.

Supplementary Data

The following data are provided to comply with certain disclosure requirements of the Securities and Exchange Commission (SEC) of the United States.

Canadian and United States Accounting Principles

The consolidated financial statements of Canadian Pacific have been prepared in accordance with generally accepted accounting principles (GAAP) in Canada, as promulgated by the Canadian Institute of Chartered Accountants. Over the years, a number of differences have developed between Canadian and United States GAAP. For the information of the Corporation's United States shareholders, the major differences are described below and on the following page, and their effect on Canadian Pacific's operating income and net income is summarized on page 99. The effect on the Statement of Changes in Consolidated Financial Position is not significant, except that dividends are treated as a financing activity in the Statement of Changes in Consolidated Financial Position under United States GAAP. The significant effect on the 1998 Consolidated Balance Sheet, had it been prepared under United States GAAP and excluding comprehensive income adjustments, would be a decrease of other assets, deferred income taxes and retained income by approximately $276.8 million, $199.2 million and $169 million, respectively, and an increase of deferred liabilities of $97.3 million. The significant effect on the 1997 Consolidated Balance Sheet, had it been prepared under United States GAAP and excluding comprehensive income adjustments, would be a decrease of other assets and retained income by approximately $195.2 million and $37.9 million, respectively, and an increase of net properties and deferred liabilities of $204.5 million and $36.2 million, respectively. If comprehensive income adjustments are included, the significant effect on the Consolidated Balance Sheet, in addition to those above, would be to decrease foreign currency translation adjustments by $187 million (1997 – $77 million), and increase deferred taxes and accumulated other comprehensive income by $64.2 million (1997 – $36.7 million) and $113.7 million (1997 – $40.3 million), respectively.

During 1997, new capitalization and reporting policies were adopted in order to present Canadian Pacific's railway results on a basis consistent with other North American railways. In accordance with Canadian GAAP, the effect of the changes has been applied retroactively and the financial statements of prior periods have been restated. Under United States GAAP, such restatements are not acceptable and the cumulative effect of the change, based on retroactive computation, is included in net income of the period of the change.

The full cost methods of accounting for conventional oil and gas operations promulgated under Canadian and United States GAAP differ in the following respect. Ceiling test calculations are performed by comparing the net book value of conventional petroleum and natural gas properties with the future net revenues expected to be generated from proven developed reserves, discounted at 10% for United States reporting purposes, and undiscounted for Canadian reporting. Any excess of net book value over future net revenues is recognized as additional depletion expense in both reporting jurisdictions.

Canadian and United States Accounting Principles (continued)

Canadian Pacific follows the Canadian method of accounting for income taxes, described as the deferral method, focusing on differences arising between financial statement income and taxable income. The method followed under United States GAAP, described as the liability method, focuses on differences between the book and tax value of assets and liabilities. In Canada, the income taxes are recorded using tax rates and regulations applicable in the year and are not changed in future years even though tax rates and regulations may change. In the United States, the tax liability is calculated using enacted future tax rates and regulations and is adjusted in future years if those tax rates and regulations are changed.

Canadian Pacific follows the Canadian practice of deferring and amortizing unrealized exchange gains and losses related to long term monetary foreign currency assets and liabilities, whereas under United States GAAP such gains and losses are included in income immediately.

The principal difference between Canadian and United States GAAP in accounting for pension costs is in the choice of discount rate used for computing the benefit obligation and the service and interest cost components of net periodic pension expense. Under Canadian GAAP, the discount rate used represents management's best estimate of the long term rate of return on pension fund assets, whereas under United States GAAP, the discount rate reflects the rate at which pension benefits can be effectively settled at the date of the financial statements. The impact of this difference on Canadian Pacific's pension expense is included in the following table. The impact of the difference on the funded status of Canadian Pacific's plans is not material.

Canadian Pacific follows the Canadian practice of expensing costs related to post retirement health care and life insurance benefits when they are paid, whereas under the United States accounting standard these costs, based on the terms of the plan, are recognized on an accrual basis during the years the plan participants provide the services.

As a result of previous differences between Canadian and United States GAAP, the carrying value for assets disposed of as discontinued differed and, consequently, gains and losses on disposal differ.

United States GAAP requires the disclosure, as other comprehensive income, of changes in equity during the period from transactions and other events from non-owner sources. Canadian GAAP does not require similar disclosure. Other comprehensive income arose from foreign currency translation and minimum pension liability adjustments.

On June 30, 1998, the FASB issued Statement No. 133 "Accounting for Derivative Instruments and Hedging" effective January 1, 2000. Canadian Pacific has not adopted the new standard as at December 31, 1998. The impact of FASB Statement No. 133 on Canadian Pacific's consolidated financial statements is not determinable at this time.

Canadian and United States Accounting Principles (continued)

For the year ended December 31 *(in millions, except amounts per share)*	1998	1997	1996
Operating income			
Canadian GAAP	**$ 1,441.7**	$ 1,765.7	$ 1,467.0
United States GAAP	**1,417.7**	2,430.8	1,450.1
Income from continuing operations			
Canadian GAAP	**801.3**	946.7	840.0
United States GAAP	**677.3**	1,317.1	884.0
Net income			
Canadian GAAP	**801.3**	1,255.8	869.1
United States GAAP	**677.3**	1,626.2	1,071.0
Earnings per Common Share			
Income from continuing operations:			
Canadian GAAP	**2.39**	2.74	2.44
United States GAAP	**2.02**	3.81	2.57
Net income:			
Canadian GAAP	**2.39**	3.64	2.52
United States GAAP	**2.02**	4.71	3.11

The following is a reconciliation of net income under Canadian GAAP to net income under United States GAAP:

For the year ended December 31 *(in millions, except amounts per share)*	1998	1997	1996
Net income – Canadian GAAP	**$ 801.3**	$ 1,255.8	$ 869.1
Increased (decreased) by:			
Oil and gas	**19.2**	1.8	25.4
Foreign exchange	**(92.2)**	(49.7)	54.6
Pension costs	**11.0**	33.5	50.8
Post retirement benefits	**(12.9)**	(8.0)	(9.3)
Prior period adjustment due to change in accounting policy	**–**	590.0	–
Reverse restatement due to change in accounting policy	**–**	–	(40.0)
Other	**(30.0)**	44.8	(14.8)
Discontinued operations	**–**	–	158.0
Adjusted net income before tax	**696.4**	1,868.2	1,093.8
Deferred income taxes	**(19.1)**	(242.0)	(22.8)
Net income – United States GAAP	**$ 677.3**	$ 1,626.2	$ 1,071.0
Other comprehensive income:			
Foreign currency translation adjustments	**$ 109.9**	$ (11.8)	$ (106.0)
Minimum pension liability	**(9.1)**	1.0	0.7
Other comprehensive income before tax	**100.8**	(10.8)	(105.3)
Deferred income taxes	**(27.4)**	3.0	47.6
Other comprehensive income	**73.4**	(7.8)	(57.7)
Comprehensive income	**$ 750.7**	$ 1,618.4	$ 1,013.3

Quarterly Financial Information (unaudited)

Statement of Consolidated Income

For the three months ended				1998
(in millions, except amounts per share)	March 31	June 30	Sept. 30	Dec. 31
Revenues	$ 2,370.3	$ 2,421.9	$ 2,504.1	$ 2,854.7
Cost and expenses:				
Cost of goods sold and services	1,508.9	1,530.9	1,534.7	1,857.6
Selling, general and administrative	287.8	274.7	300.8	329.9
Depreciation, depletion and amortization	256.1	260.6	276.5	290.8
	2,052.8	2,066.2	2,112.0	2,478.3
Operating income	317.5	355.7	392.1	376.4
Interest expense, net	53.7	56.1	65.2	75.7
Non-operating (income) expense	11.0	46.7	56.8	(37.7)
Income before income taxes and minority interest	252.8	252.9	270.1	338.4
Income tax expense	83.9	77.8	63.1	68.1
Minority interest share of income of subsidiaries	6.0	4.5	2.2	7.3
Income from continuing operations	162.9	170.6	204.8	263.0
Discontinued operations	–	–	–	–
Net income	$ 162.9	$ 170.6	$ 204.8	$ 263.0
Earnings per Common Share:				
Income from continuing operations	$ 0.48	$ 0.51	$ 0.61	$ 0.79
Net income	$ 0.48	$ 0.51	$ 0.61	$ 0.79

Non-operating income includes the following unrealized foreign exchange gains (losses): March 31 – $17.3 million; June 30 – $(47.8) million; September 30 – $(36.9) million; December 31 – $6.7 million.

Quarterly Financial Information (unaudited) (continued)

Statement of Consolidated Income

For the three months ended				1997
(in millions, except amounts per share)	March 31	June 30	Sept. 30	Dec. 31
Revenues	$ 2,184.5	$ 2,279.2	$ 2,354.1	$ 2,742.2
Cost and expenses:				
Cost of goods sold and services	1,416.9	1,343.9	1,386.6	1,682.5
Selling, general and administrative	237.4	245.5	244.4	274.4
Depreciation, depletion and amortization	224.2	227.4	247.0	264.1
	1,878.5	1,816.8	1,878.0	2,221.0
Operating income	306.0	462.4	476.1	521.2
Interest expense, net	53.0	49.6	43.9	48.3
Non-operating (income) expense	15.0	21.7	13.7	(26.0)
Income before income taxes and minority interest	238.0	391.1	418.5	498.9
Income tax expense	60.6	133.7	151.7	211.0
Minority interest share of income of subsidiaries	18.1	9.2	6.3	9.2
Income from continuing operations	159.3	248.2	260.5	278.7
Discontinued operations	23.2	14.4	271.5	–
Net income	$ 182.5	$ 262.6	$ 532.0	$ 278.7
Earnings per Common Share:				
Income from continuing operations	$ 0.46	$ 0.72	$ 0.75	$ 0.81
Net income	$ 0.53	$ 0.76	$ 1.54	$ 0.81

Operating income includes a gain on sale of KCCL in the second quarter of $54 million, and gains on sale of Molson Centre lease of $37.8 million and a portion of the St. Lawrence & Hudson line of $42.3 million in the fourth quarter.

Non-operating income for the fourth quarter includes a $211 million gain on sale of business hotels, and a $140 million provision for hedging losses and information technology costs.

Income tax expense for the fourth quarter includes a $35 million general tax provision.

Ten-Year Summary

(dollars in millions, except amounts per share)	1998	1997	1996	1995
Revenues				
Continuing operations	**$ 10,151.0**	$ 9,560.0	$ 8,471.3	$ 7,331.3
Operating income (loss) from:				
Transportation	**$ 897.2**	$ 947.7	$ 713.9	$ (618.3)
Energy	**365.6**	681.7	637.3	482.9
Hotels and Real Estate	**178.9**	136.3	115.8	96.9
	$ 1,441.7	$ 1,765.7	$ 1,467.0	$ (38.5)
Income (loss) from continuing operations	**$ 801.3**	$ 946.7	$ 840.0	$ (256.4)
Net income (loss)	**$ 801.3**	$ 1,255.8	$ 869.1	$ (786.9)
United States GAAP				
Income (loss) from continuing operations	**$ 677.3**	$ 1,317.1	$ 884.0	$ (313.8)
Net income (loss)	**$ 677.3**	$ 1,626.2	$ 1,071.0	$ (716.3)
Total Assets	**$ 19,669.4**	$ 17,331.9	$ 15,805.9	$ 16,555.7
Total capitalization				
Total long term debt	**$ 3,398.0**	$ 2,796.0	$ 3,384.6	$ 4,909.8
Perpetual 4% Consolidated Debenture Stock	**64.6**	59.6	57.2	186.6
Minority shareholders' interest in subsidiary companies	**357.7**	350.6	321.6	311.1
Shareholders' equity	**7,998.0**	7,573.4	6,727.8	6,129.9
	$ 11,818.3	$ 10,779.6	$ 10,491.2	$ 11,537.4
Per Common Share:				
Income (loss) from continuing operations:				
Canadian GAAP	**$ 2.39**	$ 2.74	$ 2.44	$ (0.75)
United States GAAP	**$ 2.02**	$ 3.81	$ 2.57	$ (0.92)
Net income (loss):				
Canadian GAAP	**$ 2.39**	$ 3.64	$ 2.52	$ (2.30)
United States GAAP	**$ 2.02**	$ 4.71	$ 3.11	$ (2.10)
Dividends	**$ 0.54**	$ 0.48	$ 0.48	$ 0.36
Number of Common Shares *(millions)*				
Year end	**332.7**	340.7	346.9	342.3
Average	**335.8**	345.4	344.4	342.1
Rate of return on average shareholders' equity	**10.3%**	17.6%	13.5%	(11.9%)
Debt:equity ratio	**29 : 71**	26 : 74	33 : 67	44 : 56

1994	1993	1992	1991	1990	1989
$ 6,367.1	$ 5,637.2	$ 4,927.4	$ 5,027.6	$ 5,055.8	$ 4,680.0
$ 453.1	$ 390.5	$ (241.5)	$ 101.0	$ 467.1	$ 383.8
505.8	397.9	321.7	184.5	424.0	297.6
72.7	57.1	50.0	24.5	58.2	53.9
$ 1,031.6	$ 845.5	$ 130.2	$ 310.0	$ 949.3	$ 735.3
$ 485.6	$ 364.1	$ (108.2)	$ (256.4)	$ 437.9	$ 325.7
$ 427.7	$ (155.5)	$ (443.2)	$ (878.7)	$ 390.4	$ 780.3
$ 414.3	$ 398.0	$ (265.1)	$ (384.0)	$ 380.6	$ 311.1
$ 289.0	$ (117.8)	$ (693.9)	$ (1,037.4)	$ 320.3	$ 768.3
$ 17,368.7	$ 17,528.4	$ 20,607.0	$ 20,908.0	$ 20,482.1	$ 19,244.6
$ 4,883.8	$ 6,063.3	$ 7,715.9	$ 7,215.3	$ 4,564.4	$ 4,256.4
194.5	178.1	172.4	176.4	180.1	162.9
291.1	265.6	815.2	867.0	1,043.3	1,238.8
7,060.9	6,242.7	6,490.8	6,883.8	7,962.7	7,897.2
$ 12,430.3	$ 12,749.7	$ 15,194.3	$ 15,142.5	$ 13,750.5	$ 13,555.3
$ 1.44	$ 1.14	$ (0.34)	$ (0.81)	$ 1.37	$ 1.03
$ 1.23	$ 1.25	$ (0.83)	$ (1.21)	$ 1.19	$ 0.98
$ 1.27	$ (0.49)	$ (1.39)	$ (2.76)	$ 1.23	$ 2.46
$ 0.86	$ (0.37)	$ (2.18)	$ (3.26)	$ 1.00	$ 2.42
$ 0.32	$ 0.32	$ 0.32	$ 0.63	$ 0.92	$ 0.84
341.8	319.4	319.1	318.7	318.2	318.2
337.5	319.2	318.8	318.5	318.5	317.3
6.4%	(2.4%)	(6.6%)	(11.8%)	4.9%	10.2%
41 : 59	49 : 51	52 : 48	49 : 51	35 : 65	33 : 67

Geographic Distribution of Net Property Investment

Properties at Cost, Less Depreciation

At December 31, 1998 (in millions)	Canadian Pacific Railway	CP Ships	PanCanadian Petroleum	Fording	Canadian Pacific Hotels	Other	Total	Percent of Total
Canada								
Atlantic Provinces and Offshore	$ 0.5	$ –	$ 103.5	$ –	$ 4.0	$ –	$ 108.0	1%
Quebec	32.2	51.8	0.3	–	99.6	–	183.9	1%
Ontario	838.4	1.0	47.6	–	61.2	117.2	1,065.4	7%
Manitoba	286.7	–	0.3	–	–	–	287.0	2%
Saskatchewan	507.3	–	575.8	1.1	–	–	1,084.2	7%
Alberta	910.8	–	3,949.2	132.6	268.7	36.6	5,297.9	35%
British Columbia	1,440.2	–	123.4	491.4	83.2	35.5	2,173.7	15%
N.W.T., Yukon	–	–	19.0	–	–	–	19.0	–
Transportation Equipment	1,258.8	–	–	–	–	–	1,258.8	8%
	5,274.9	52.8	4,828.8	625.1	516.7	189.3	11,477.9	76%
Outside Canada								
United States	1,717.6	6.8	142.2	65.1	387.5	–	2,319.2	15%
Other	–	262.0	325.1	189.2	393.5	5.6	1,175.4	8%
Ocean Ships	–	137.4	–	–	–	–	137.4	1%
	1,717.6	406.2	457.6	254.3	781.0	5.6	3,632.0	24%
	$ 6,992.5	$ 459.0	$ 5,286.4	$ 879.4	$ 1,297.7	$ 194.9	$15,109.9	100%

Shareholder Information

Common Share Market Prices

Toronto Stock Exchange	1998		1997	
(Canadian Dollars)	**High**	**Low**	High	Low
First Quarter	**44.55**	**31.90**	37.60	32.65
Second Quarter	**45.90**	**39.10**	40.35	31.80
Third Quarter	**41.00**	**26.55**	43.45	38.30
Fourth Quarter	**37.05**	**28.45**	43.85	35.50
Year	**45.90**	**26.55**	43.85	31.80

New York Stock Exchange	1998		1997	
(U.S. Dollars)	**High**	**Low**	High	Low
First Quarter	**31.38**	**22.38**	27.88	23.88
Second Quarter	**31.50**	**26.63**	29.13	22.63
Third Quarter	**28.44**	**17.94**	31.44	28.06
Fourth Quarter	**24.25**	**17.88**	31.69	24.75
Year	**31.50**	**17.88**	31.69	22.63

Shareholder Administration

The Trust Company of Bank of Montreal, with transfer facilities in Montreal, Toronto, Calgary, Vancouver and in London, England, through its agent, Computershare Services plc, serves as transfer agent and registrar for the Common Shares. The Bank of Montreal Trust Company serves as transfer agent and registrar for the Common Shares in New York.

For information concerning dividends, or for change in share registration or address, call 1-800-332-0095 or (514) 877-2584, or write to:

The Trust Company of Bank of Montreal
129 Saint-Jacques Street, "A" Level North
Montreal, Quebec
Canada H2Y 1L6

Shareholder Services

Shareholders having inquiries or wishing to obtain copies of the Corporation's Annual Information Form should write to:

Shareholder Services
Office of the Corporate Secretary
Canadian Pacific Limited
1800 Bankers Hall East,
855 - 2nd Street S.W.
Calgary, Alberta
Canada T2P 4Z5

Market for Securities

The Common Shares of Canadian Pacific Limited are listed on the Montreal, Toronto, Alberta, Vancouver and New York stock exchanges.

Trading Symbol
Toronto and New York stock exchanges – CP

Dividend Reinvestment and Share Purchase Plan
Eligible holders of Canadian Pacific Limited Common Shares may acquire new Common Shares through reinvesting cash dividends and/or investing optional cash payments, without paying brokerage commissions or administrative charges. An information circular providing details of the Plan may be obtained from The Trust Company of Bank of Montreal or from Shareholder Services at Canadian Pacific Limited.

Direct Deposit of Dividends
Shareholders are offered the option of having their Canadian dollar dividends directly deposited into their personal bank accounts in Canada on the dividend payment dates. Shareholders receiving their dividends in Canadian currency, as well as those shareholders whose dividends are not reinvested through the Dividend Reinvestment and Share Purchase Plan, may obtain a direct deposit enrolment form from The Trust Company of Bank of Montreal or from Shareholder Services at Canadian Pacific Limited.

Duplicate Annual Reports
While every effort is made to avoid duplication, some Canadian Pacific Limited registered shareholders may receive multiple copies of shareholder information mailings such as this Annual Report. Registered shareholders who wish to consolidate any duplicate accounts which are registered in the same name are requested to write to The Trust Company of Bank of Montreal.

Investor Relations
Institutional investors, brokers, security analysts and others desiring copies of Canadian Pacific's Financial and Operating Information Booklet or other financial information should contact:

Sheila M. McIntosh
Vice-President
Corporate Communications and Investor Relations
Canadian Pacific Limited
1800 Bankers Hall East
855 - 2nd Street S.W.
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Web Site
Visit our web site at www.cp.ca

Statement of Corporate Governance Practices

Canadian Pacific's Board of Directors and the members of its management are committed to a high standard of corporate governance. Effective corporate governance calls for the establishment of processes and structures that contribute to the sound direction and management of the Corporation's business with a view to enhancing shareholder value. The Board believes that the corporate governance practices summarized below are consistent with these objectives.

The Board consists of 15 directors, 14 of whom are unrelated. The only related director is the Chairman, President and Chief Executive Officer. The number of directors constituting the Board has been reduced over the past 13 years from 28 members to its current 15. The Board believes that this number is appropriate and allows the Board to deliberate effectively.

Although D. P. O'Brien is both Chairman of the Board and Chief Executive Officer of the Corporation, the fact that he occupies both offices does not, in the opinion of the Board, impair its ability to act independently of management. The opinion is based on the proportion of unrelated to related directors and the fact that an unrelated director, the Chairman of the Corporate Governance and Nominating Committee, has been designated lead director.

The Board assumes responsibility for the stewardship of the Corporation and, in discharging that responsibility, it annually reviews and approves a long term strategic plan, an annual financial budget, as well as the consolidated financial statements. It also considers and, if appropriate, approves major acquisitions and dispositions.

At this time, the Board has established six committees to assist it in carrying out its responsibilities.

The Executive Committee of the Board is composed of a majority of unrelated directors. Its mandate is to exercise powers of the Board, between meetings of the Board, with certain exceptions prescribed by law and to meet with the CEO to discuss significant policy issues, business plans, acquisitions and divestitures.

The Audit Committee consists entirely of unrelated directors. It is responsible for overseeing the Corporation's internal controls and management information systems, as well as identifying the principal risks of the Corporation's businesses and the systems in place to manage these risks. The committee also reviews with management and the internal and external auditors the Corporation's financial reporting procedures in connection with the annual audit and the preparation of the financial statements.

The Management Resources and Compensation Committee is composed entirely of unrelated directors. It is responsible for making recommendations to the Board on management succession planning within the Corporation and its major subsidiaries. It is also responsible for recommending to the Board the fees to be paid to directors and the compensation to be paid to management. It assesses the performance of the Chief Executive Officer and determines his compensation based on the attainment of objectives set by the Board that are consistent with the Corporation's strategic plan and that are reflected in the performance criteria of the Corporation's short and long term incentive plans.

The Corporate Governance and Nominating Committee is composed entirely of unrelated directors and is charged with responsibility for all matters relating to corporate governance. These responsibilities include recommending candidates for nomination, appointment, election and re-election to the Board and its Committees, assessing Board performance, and determining the most appropriate orientation and education program for new Board members. Given that the offices of Chairman and Chief Executive Officer are held by the same person, the Board meets without management present when the Board deems appropriate. Directors may, in circumstances considered appropriate by this Committee, engage the services of outside advisors at the Corporation's expense.

The Environmental and Safety Committee is composed entirely of unrelated directors. It is responsible for making recommendations to the Board on environmental and safety issues and for making reports to the Board on the effectiveness of the Corporation's response to environmental and safety issues, on the management risks associated with these issues, and on the implementation of the environmental and safety policy statement adopted by the Board.

The Pension Trust Fund Committee is composed of a majority of unrelated directors. It is responsible for overseeing the operation and administration of the Corporation's pension plans and the investment policies and management of the pension trust funds.

The Board of Directors believes it is important to maintain effective communication with its shareholders. To this end, it reviews the Corporation's Annual Report, Management's Discussion and Analysis, Management Proxy Circular, Annual Information Form, quarterly financial statements, and press releases on major developments, in each case before they are distributed. The Corporation also maintains shareholder and investor relations' services to respond to all shareholder inquiries. Telephone numbers are provided on pages 105 and 106 of this Annual Report.

Board of Directors

[1] Stephen E. Bachand
President and Chief Executive Officer
Canadian Tire Corporation, Limited
Toronto

[1,3,5] Dian Cohen, C.M., LL.D.
President
Dian Cohen Productions Ltd.
Ayers Cliff, QC

[3] M. James Fielding
Chairman of the Board
Alexander Centre Industries Limited
Sudbury

[3] The Hon. Peter Lougheed, P.C., C.C., Q.C.
Partner, Law Firm of Bennett Jones
Calgary

[1,5] Angus A. MacNaughton
President
Genstar Investment Corporation
Foster City, CA

[1,2,4,6] John D. McNeil
Chairman
Sun Life Assurance Company of Canada
Toronto

[2,4,5,6] Stanley A. Milner, A.O.E., LL.D.
President and Chief Executive Officer
Chieftain International Inc.
Edmonton

[1,5] James E. Newall, O.C.
Chairman
NOVA Chemicals Corporation
Calgary

[4,6] David P. O'Brien
Chairman, President and Chief Executive Officer
Canadian Pacific Limited
Calgary

[2,4,6] James A. Pattison, O.C.
Chairman, President and Chief Executive Officer
Jim Pattison Group Inc.
Vancouver

[3] Michael E.J. Phelps, LL.B., LL.M., LL.D.
Chairman and Chief Executive Officer
Westcoast Energy Inc.
Vancouver

[5] Ronald D. Southern, C.M., C.B.E., LL.D.
Chairman and Chief Executive Officer
ATCO Ltd. and Canadian Utilities Limited
Calgary

William W. Stinson
Chairman of the Executive Committee
United Dominion Industries Limited
Calgary

[2,4,5,6] Allan R. Taylor, O.C.
Retired Chairman and Chief Executive Officer
Royal Bank of Canada
Toronto

[3] The Rt. Hon., The Viscount Weir
Chairman
BICC, PLC
Glasgow, Scotland

[1] Member of Audit Committee
[2] Member of Corporate Governance and Nominating Committee
[3] Member of Environmental and Safety Committee
[4] Member of Executive Committee
[5] Member of Management Resources and Compensation Committee
[6] Member of Pension Trust Fund Committee

Directorate

At the Annual Meeting held on April 21, 1998, Lloyd I. Barber, C.C., S.O.M., Ph.D. and A. S. (Peter) Kingsmill, Q.C. retired as directors of the Corporation. Dr. Barber was appointed a director in 1983 and during his tenure served on the Nominating, Management Resources, and Environmental and Safety Committees of the Board. Mr. Kingsmill was appointed a director in 1984 and was a member of the Environmental and Safety Committee. The directors desire to record their recognition of the notable contributions made to the affairs of the Corporation by these long-standing directors.

Officers

David P. O'Brien
Chairman, President and
Chief Executive Officer
Calgary

Michael A. Grandin
Executive Vice-President
and Chief Financial Officer
Calgary

William R. Fatt
Executive Vice-President
Toronto

Ronald K. Gamey
Executive Vice-President
Calgary

Edward J. Dato
Vice-President Corporate
Calgary

Robert B. Hodgins
Vice-President and Treasurer
Calgary

Alison T. Love
Vice-President Law, General Counsel
and Corporate Secretary
Calgary

Sheila M. McIntosh
Vice-President Corporate
Communications
and Investor Relations
Calgary

Norman E. Wale
Vice-President Corporate Research
and Development
Montreal

A copy of the 1998 annual report of each of the following businesses can be obtained by writing to its Secretary:

Canadian Pacific Railway Company

Suite 500
Gulf Canada Square
401 - 9th Avenue S.W.
Calgary, Alberta T2P 4Z4
www.cpr.ca

PanCanadian Petroleum Limited

PanCanadian Plaza
P.O. Box 2850
Calgary, Alberta T2P 2S5
www.pcp.ca

Fording Inc.

205 - 9th Avenue S.E.
Calgary, Alberta T2G 0R4

Canadian Pacific Hotels & Resorts Inc.

One University Avenue
Suite 1400
Toronto, Ontario M5J 2P1
www.cphotels.com

Si vous désirez vous procurer la version française du présent rapport, veuillez vous adresser à la vice-présidente, Contentieux, conseillère juridique générale et secrétaire générale, Canadien Pacifique Limitée
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855 Second Street S.W.
Calgary (Alberta) T2P 4Z5

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CANADIAN PACIFIC

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